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TRANSPORTATION

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ROYAL COMMISSION ON TRANSPORTATION

Monday, March 13, 1950.

Index Page #113

	<u>Page</u>
<u>PROFESSOR J. L. McDOUGALL</u> - Recalled. Examination by Mr. Evans resumed - - - - -	17763
Noon adjournment - - - - -	17838
<u>PROFESSOR J. L. McDOUGALL</u> - Recalled. Examination by Mr. Evans resumed - - - - -	17839
Adjournment - - - - -	17909

- - - - -

ROYAL COMMISSION ON TRANSPORTATION

OTTAWA, ONTARIO
MONDAY
MARCH 13, 1950.

THE HONOURABLE W.F.A. TURGEON, K.C., LL.D.	-	CHAIRMAN
HAROLD ADAMS INNIS	-	COMMISSIONER
HENRY FORBES ANGUS	-	COMMISSIONER

G.R. Hunter
Secretary

P.L. Belcourt
Asst. Secretary

COUNSEL APPEARING:-

F.M. Covert, K.C.	}	Royal Commission on Transportation
G.C. Desmarais, K.C.		
H.E. O'Donnell, K.C.	}	Canadian National Railways
H.C. Friel, K.C.		
F.C.S. Evans, K.C.	}	Canadian Pacific Railway
I.D. Sinclair		
C.D. Shepard	)	Province of Manitoba
M.A. MacPherson, K.C.	)	Province of Saskatchewan
J.J. Frawley, K.C.	)	Province of Alberta
F.D. Smith, K.C.	}	Province of Nova Scotia; Transportation Commission of the Maritime Board of Trade.
J. Paul Barry		
C.W. Brazier		
J.O.C. Campbell, K.C.	)	Province of Prince Edward Island.

Ottawa, Ontario
Monday, March 13, 1950.

M O R N I N G S E S S I O N

---The Commission resumed at 10.30 a.m.

PROFESSOR J. L. McDOUGALL - Recalled

EXAMINATION BY MR. EVANS:- (Cont.)

THE CHAIRMAN: Very well, Mr. Evans.

MR. EVANS: Q. Mr. McDougall, at the close of Friday you had been giving us your views as to the reasons against the removing of geographic disadvantages through the agency of transport charges. Having given us an indication of what you do not believe in, would you be good enough to indicate the principles that you believe in as necessary to make transportation the greatest possible service to the country?

THE CHAIRMAN: Will you speak louder, Mr. Evans?

MR. EVANS: I asked Dr. McDougall to say, having given us what he did not believe in, what he did believe in as to the proper principles to make transportation of the greatest possible service to Canada.

THE WITNESS: Why, I believe that transportation should be provided on some basis broadly related to the entire cost of producing it, modified by consideration of the ability of various forms of traffic to bear those costs. That any consideration of individual rates seems to give a picture of an unbearable complication; but it seems to me that any closer study of rate structure as a whole will show that it is in fact a coherent and consistent structure built up on that basis, and that nothing so complicated as that can be perfect, and therefore ought to be subject to continued study, aiming at its improvement. I believe that

Canada will be better off if it sticks to the broad principles and refuses to be lead off into sentimental attempts ; to substitute local political pressures for the hard but enduring economic principles as a basis for freight rate structure.

MR. EVANS: Q. I am going to read you a couple of paragraphs from the Company's outline submission, at page 36, paragraphs 31 and 32:-

"31. Canadian Pacific submits that national transportation policy should aim at the maintenance of facilities adequate to serve at all times a freely growing national economy. Total transportation costs should be as small a part as possible of total national income and should make no unnecessary or uneconomic use of labour or materials.

32. Further, if it is decided that any industry or any part of Canada is to be assisted at the cost of the whole nation, subsidies, if and when given, should be certain in their effect and flexible in their administration. Transportation subsidies are, by their very nature, unable to meet these tests and should therefore not be resorted to."

Now, Mr. McDougall, you are familiar with the criticisms that have been made to the present freight rate structure, which has been made by different parts of Canada. Do you find any general theory pervading these criticisms?

A. Well, I think, sir, that to a remarkable degree those who make those criticisms make two assumptions: first,

to assume that there is something unjust in a situation which leads to some part of Canada developing less rapidly than others; and second, in some fashion the railways are chiefly responsible.

Q. Would you like to comment on that attitude?

A. It is again a case of everybody wanting his bread with jam on both sides. The people of Saskatchewan, for example, seem inclined to resent the fact that there is not as much industrial development there as there is in the peninsula in Western Ontario; but they leave out consideration of the fact that Saskatchewan has enormous agricultural production in special lines, which cannot be duplicated in the industrial areas in Western Ontario. That, I think, is typical. It is a protest against a condition which is in a large part a consequence of natural advantages in Saskatchewan in agriculture, and which do not result from transportation factors at all.

Q. You have said that it is typical of these criticisms. Would you comment generally in that connection on, say, the position in the Maritimes?

A. The Maritimes have created a very stable society, productive as we all know of a very fine type of citizen; but as the Maritime Provinces are limited in area, and they have only certain forms of natural resources, I think it is inevitable that their economic and sociological conditions will be very different from that of British Columbia, or of the Edmonton district, where natural wealth is available on quite another scale. And this has nothing to do with transportation.

Q. To what do you attribute that?

A. Part of it, perhaps the most powerful part is the

uncomprehended and unreasoning impatience. The Commission will remember Professor Stewart suggested that a proper comparison would be between Alberta and Kansas.

MR. EVANS: That will be found at page 1994, my lord.

THE WITNESS: Now, Alberta in fact is today as far ahead of Kansas, as it was a generation ago, although there is more than a generation difference in the periods of settlement. Even in their greatest discontent of present conditions - -

THE CHAIRMAN: Q. You mean as Kansas was a generation ago?

A. Yes; that is when there is more than the difference of a generation in periods of settlement. The proper comparison of Alberta today is with Kansas at least a generation back, and even in their greatest discontent with present conditions the people of Alberta do not use the violent language of the Kansas populists. The position of Alberta's economy today is so much better relatively and absolutely than that of Kansas a generation ago, that there is substantially no reason to envy Kansas; if Alberta's past is relatively good her future is still better. There is every expectation that the province will show an economic development which will in time outrun that of Kansas.

MR. EVANS: Q. What is that part of the trouble attributable to?

A. I think they are forgetful of dates; they make a direct comparison between a province in Canada and a major state in the United States, and they forget that they two did not start at the same time. What is more important is the failure to recognize that economic

development is a process taking place over a period of time and not a sudden and causeless phenomenon. A balanced economic development is not something that can be whistled out of the vast deep like the Russian five-year plan; it takes place slowly, day by day; and out of respect for process comes results. People who look only at the results prove by that very fact their lack of knowledge of process from which alone the desired results can flow.

Q. Do I gather from your answer that your opinion is that discontent of material progress in Canada is not justified?

A. Well, when you consider the relative development, that is, relative progress, and not absolute levels, as measured by population increase and other indices, it seems to me we should in fact be optimists. There is not a part of Canada which has not been for many years now showing economic expansion in excess of comparable areas of the United States.

Q. Would you say, for example, that the Prairie Provinces had shown a reasonable rate of industrial and commercial expansion?

A. Yes, sir. I am not going to take you all through the exhibits, comparing economic progress in the Prairie Provinces to those in the Spring Wheat States. The Prairie Provinces show an increased percentage of employees of manufacturing industries in Canada, while the Spring Wheat States have for many years shown a decrease in the percentage of manufacturing workers.

Q. Have you anything particular in mind in that connection?

A. Yes, I would like to draw attention to the development

of modern, urban communities in the two areas. Where in a corresponding area in the United States will you find an urban community of the size of Edmonton, Calgary, Saskatchewan or Regina? Omaha is certainly no better by any standard than is Winnipeg, which is a corresponding community in a geographic sense. It think it is time Canadians dropped their inferiority complex.

In that connection I point at least to the Maritimes, and say that while the population is increasing slowly, it is increasing more rapidly than in the corresponding states in New England.

Q. I assume you do not forecast a duplication in Canada of the growth of the United States?

A. Absolutely not. I am discussing it wholly in relative terms; the total resources and population of the United States are much larger than those of Canada - about eleven times in population, and more than that in developed economic production. That means that there are some forms of development in the United States which cannot be duplicated in Canada; certainly not now, and perhaps not ever. But looking at two countries, considering the type, the nature and desirability of their economic resources, I feel that Canadians can hold up their heads in pride. There just is not the ground for that kind of crepe hanging to which many of us are addicted.

Q. Now, at page 39 of Part I, this paragraph appears:-

"This is not solely the result of
opening new lands."

We had been speaking there in the Brief about the increase of population in Canada being relatively more rapid than in

the United States. The paragraph reads:-

"It is very much more the result of the general development of the world economy, making it economical to increase the development of Canadian resources. So long as the structure of world trade remains strong it is quite probable that Canada will continue to grow a little more rapidly than does the United States".

Would you please comment on that paragraph?

A. I think, sir, that that is a simplification; that a world which needs food stuffs and raw materials in increasing volume has been turning in an increasing degree to Canada as its source. Canada is in a very powerful position in the expanding world economy, and by no means only as a source of raw materials. Our people have shown a great ability in developing secondary industry, and as long as the world economy continues to expand, it is certain that Canada will continue to grow rapidly in population, in production and the establishment of a high standard of living.

Q. To what then do you attribute these constant references to the terribly depressing conditions on the Prairie fifteen or twenty years ago?

(Page 17770 follows)

A. Well, those references are entirely justified. It was terrible. It was a combination of two things -- an adverse climatic cycle and adverse prices. The prairie provinces went through an appalling experience of poverty, but, although too many Canadians do not realize it, their poverty was reflected in general depression throughout the country. This did not result from transportation conditions; it arose from a world-wide breakdown of commerce. In view of the great increase in secondary production in Canada, and particularly the development of new forms of natural resources in the prairie provinces, it is quite unnecessary for us to look back to those days. We have every reason to look forward to a great expansion of the Canadian economy, and particularly that of the prairie provinces.

Q. Then I am going to read to you from page 45, beginning at a paragraph near the end of the page, the last complete paragraph:

"The suggestion is made that the economic independence of this nation has forced trade into East and West channels, when North and South movement would be normal, with the result that Canadian producers and consumers suffer from improperly high transportation charges.

Were this the case, it must be clear that the blame could not lie on Canadian railways, nor would there be justice or expediency in forcing Canadian railways to make the necessary compensation for any mistakes which may have been made in tariff policy.

It is not the intention of Canadian Pacific to discuss tariff policy. The railway system was built after broad national policies were established. The railways did not initiate these policies, nor were they initiated for their benefit. Accordingly, the railways

can take no responsibility for defending them, nor the duty of examining them critically.

What can be pointed out is that there is every reason to believe that trade in Canada would still tend to move East and West not North and South in respect of many important commodities, were this country to engage in economic union with the United States.

Wheat, for example, would still flow from the wheat growing areas to the Head of the Lakes or to the Pacific Coast, if economic union were established. Wheat from the Prairie might move to Duluth, instead of Fort William and Port Arthur, or to Seattle, instead of to Vancouver. The distance of movement would be substantially the same or slightly longer, and the charge for moving a bushel of wheat would be more than doubled.

It must not be forgotten that economic union between the two nations would, among other consequences, inevitably produce transportation charges in Canada such as now exist in the United States.

It would still be the case that motor cars would move to Western Canada from the banks of the Detroit River. Freight rates on motor cars from Windsor to Prairie points are cheaper than those from Detroit to similar points South of the border. The same thing is true of agricultural machinery, and it is equally true of lumber, which moves from British Columbia to Central Canada more cheaply than does lumber from the United States Pacific Coast to the industrial areas of the Eastern and Central United States.

The illusion that traffic has been forced into unnatural East and West channels in Canada is exploded by an examination of railway maps and railway traffic

statistics of the United States. There has been the same tendency to East and West movement in that country, in the areas contiguous to Canada, and there is no reason to believe that there would have been any substantial alteration in the internal trade pattern of either of the two countries, if they had developed as a single economic unit. Notable exceptions to this might very well have been a failure to develop Canadian seaports and Canadian industrial and commercial centres to the present extent."

Now, I understand that you have examined railway maps of the United States and Canada, and that you are fully familiar with the argument developed in that portion of the brief which I have read. Would you like to comment on that, Mr. McDougall?

A. Yes. I think that examination of those railway maps will indicate that the transportation development in the northern part of the United States has been very much like that in Canada. The Great Northern, the Northern Pacific, and the Chicago, Milwaukee, St. Paul & Pacific, are all east-and-west railways. They have responded to the demands of the economy which they serve just as have the transcontinental railways in Canada. There has been no tendency to develop a north-south traffic on any great scale in that area. It is only after you get down to Kansas City that you find the transportation economy in the United States with some elements of a general north-south tendency. Your submission well develops that situation. It is one in which economic union of the two countries would not have produced a major alteration in the Canadian transportation pattern, except that the much higher U. S. freight rates would prevail in Canada.

Q. Do you know of any case in which the national

policy of Canada has tended to force trade in east-and-west channels?

A. Yes, I think there is one case. As a result of national pressure, the port of Portland, which had been used by the Grand Trunk as its winter port, was abandoned in favour of Canadian Atlantic ports.

THE CHAIRMAN: Q. Do you mean Portland, Maine?

A. Portland, Maine, yes, sir. The Maritimes, however, notwithstanding that they were the beneficiaries of this abandonment and re-routing, have complained and are complaining that they are suffering because the tariff policy forces them to look to Central Canada for their markets and their supply of manufactured goods.

MR EVANS: Q. Now, what is your view as to whether Canadian railways have done what is necessary to correct this difficulty?

A. Well, I think they have gone as far as they can to correct any disadvantage that the Maritimes suffer under. For example, the comparison was given of the rates on potatoes from Maine to Buffalo as against the rates from New Brunswick to Toronto. The Maine potato producers cannot reach the markets to the south of them in their own country at rates anything like as low as are applicable between the Maritime Provinces and Central Canada, except possibly where water competition such as exists between the Maine coast ports and Philadelphia, for example, has brought about reductions in rates.

Q. Then did you want to refer to the table at page 54 of the Appendix to Part I?

A. I think that was the one I had in mind.

Q. Is there anything you wanted to say especially about that table?

A. Well, I see there the rates from Houlton, Maine, to

Buffalo, New York, 91¢ on a 36,000-pound minimum, and from Woodstock, New Brunswick, to Toronto, Ontario, 46¢ on a 35,000-pound carload minimum.

Q. Where did you see that 46¢?

A. That is the ninth item down the page, the fourth commodity.

Q. Yes, Woodstock to Toronto; it is in the same line as the Houlton, Maine, to Buffalo, 91¢, and the corresponding rate for a similar distance in Canada. Woodstock, New Brunswick, to Toronto is 46¢; that is what you have in mind?

A. Yes.

Q. Now, I want to read you another paragraph from page 47 of Part I of the brief.

COMMISSIONER INNIS: Q. I was going to ask, you have not made any comparison as to the prices of potatoes in those particular transactions?

A. No, I have not; but, in so far as this is a railway problem and not a problem of the whole economy, I do not know what the railways can do about prices in Toronto.

Q. I am not saying they can do anything, but I am suggesting that prices of potatoes in the two regions might involve a difference.

A. Well, American potato prices are a good deal in the newspapers these days; I judge they are higher, but I do not know by how much.

Q. Well, you have not looked into that?

A. No.

MR EVANS: Q. The paragraph I am about to read follows the paragraph I finished reading a few minutes ago:

"In discussing this question with reference to Western Canada there are many references to the fact that Canadian railways pass through a wide unproductive area North of the Great Lakes. So they do, but the

burden of overcoming this disadvantage is no greater than if the alternative route through the United States south of the Great Lakes had been used. That burden has not caused railway rates between Central and Western Canada to be as high as those on the more fortunately situated railway lines in the United States. This^{is} clear from the table of rates at pp. 52-53 of the Appendix."

Now, Mr. Jefferson commented on that from the standpoint of the traffic department; would you care to comment on that paragraph?

A. Well, I think, sir, the obvious answer is the comparison of rates on the east-west movement in the two countries which are before the Commission. It is perfectly true that the Canadian railways would have had an easier time and a more profitable early life if they had run south of the Great Lakes, but the railways, not the economy in general, have carried the burden of this added cost of running through an unproductive area. The policy has paid off to a certain extent, for the unproductive area is now producing more per mile in the way of traffic than do the prairies. Canadian railways still have an extra burden which they and not the economy have to bear in this matter, but the over-all wisdom of the policy in the national interest would seem to have been demonstrated. If the outlet and inlet for traffic between Western Canada and the east were through Chicago and not through Winnipeg and the north shore of the lakes, Western Canada would not be getting as low rates as it is getting today, and the development of Canada as a nation would almost certainly have been much delayed if not completely inhibited.

Q. What do you mean by that, Mr. McDougall?

A. Well, I mean that Ontario, Quebec and the Maritimes would have been deprived of the advantages of having Western Canada in economic union with them, without Western Canada having obtained any advantage. Indeed, Western Canada under such a system would, to the extent that transportation charges are a factor, have been worse and not better off than they are at present.

Q. Well, is there any suggestion in your mind that Canadian railways have in this way been forced to accept undue burdens so that Canadian industry should be developed?

A. No, sir, there is not. There has been a burden, but I think it would be wrong to call it an undue burden. Over the long run the plan has worked out well enough. Any net disadvantage to Canadian railways does not arise from past national policy but from the delays in adjusting freight rates in this country in periods of a general increase in prices. In any event Canadian railways have no responsibility for national policy. Their business is simply to provide the country with adequate transportation facilities. Putting aside the special case of Canadian National, which arises from the history of the railways out of which it was constituted, I think it is quite notable that Canadian railways have not complained of their obligation to provide the nation with transportation services, even though they have done so more cheaply than American railways have served the United States.

Up to the outbreak of the first World War railroading was economically successful in Canada at the freight rates which prevailed. During and following that war, in striking contrast with present conditions, railway rates were allowed to rise in accordance with the general price increase. Railroading in Canada continued to be

a profitable enterprise. In accordance with general conditions freight rates were decreased after the first World War, but it was not until a general depression settled on the country that railroading in Canada became unprofitable, a condition which has continued since then with the exception of the temporary boom toward the middle of the second World War. Even during the depression Canadian railways, unlike those of the United States, did not follow a policy of increasing rates.

Q. You are referring there to the applications that we have discussed here before the Interstate Commerce Commission in 1931, 1932, and so on?

A. Yes, the successive increases that came in the 1930's.

Q. Now, do you think there is any reason to think that the business of rail transportation in Canada will be necessarily unprofitable in the future?

A. No, sir, I do not think there is any ground for thinking it will be unprofitable -- far from it. I believe that experience demonstrates that, provided railway charges for service are permitted to rise and fall when there are great general rises and falls in price levels, railroading will be profitable in Canada whenever the country is in a sound economic condition. Canadian railways have the single task of providing the nation with transportation service in the circumstances which exist at any given time. They have proven themselves capable of doing this, and with the lowest charges which exist in any modern nation.

Q. What do you consider to be the major problem of transportation in Canada today?

A. I think the major problem is that of permitting the railways to participate in national prosperity, exactly as they are compelled to share in the national difficulties.

Q. Then I am going to read to you further from the brief, beginning at the bottom of page 48 of Part I, the very last line:

"However, Canadian Pacific submits that there are grave reasons for feeling that it is not desirable to attempt to aid the economy of any area of the country by transportation subsidies.

There is no reason to believe that this method of assistance to any area encourages normal and desirable economic development in that area, and, indeed, the effect may be in quite another direction. This plan may produce the establishment in any area of industrial or other developments which are not economically justified. It may lead to an undue emphasis on the production for sale in other areas of unprocessed raw materials which, under some other plan, might contribute more effectively to economic progress were they to be processed within the area.

If it be accepted -- as was the case in the studies leading to the passing of the Maritime Freight Rates Act -- that any particular area of Canada is at a general economic disadvantage as compared with the rest of the nation, then Canadian Pacific submits that any subsidy granted by the Dominion Government for the relief of this condition should be distributed to all economic interests within the area according to their needs. In this way, there would be no tendency for the use of such a subsidy to direct the economic activities of the area in any particular direction, but all activities within the area would be given assistance where necessary.

The argument is that assistance to the economy of an area by means of a transportation subsidy tends to

stimulate those industries in whose affairs transportation costs are a large factor, in preference to those industries in whose business the burden of transportation is a small one. Such a system, while possibly stimulating certain forms of economic activity, may actually deter the creation of a fully rounded economy.

Canadian Pacific has no suggestion to make for any particular method of distributing such a subsidy, but does believe that, on full investigation and consideration, it will be decided that it should not be distributed in respect of one specific factor, such as transportation of goods within and out of the area.

The further, and fatal objection, in the opinion of Canadian Pacific, to the principle of transportation subsidies is that it can only end in vicious competition between various areas, transferring transportation costs from those who use transportation to the taxpayers at large.

If there be two areas, A and B, which trade with each other, and if the goods which A ships to B receive a subsidy in respect of transportation, to the advantage of economic development in area A, then every argument will exist for their being similar treatment applied to the shipment of goods from area B to area A. In such circumstances all that would occur would be a subsidy from the taxpayers of the two areas, as well as all taxpayers of Canada, to the transportation of goods between the two areas -- creating the unfavourable effect of all general subsidies on transportation, in the direction of causing unnecessary use of this service, and thus imposing an unfortunate burden of wasted effort on the economy as a whole."

What do you say as to the submissions of the Canadian Pacific

which I have just read?

THE CHAIRMAN: Pardon me a moment before Mr. McDougall answers. I do not know just how far you are going. Are you talking so far only of the future, or are you also aiming at what has already been done since the Maritime Freight Rates Act?

MR EVANS: No, sir; I think our brief is quite clear on that. We do not ask that the Maritime Freight Rates Act be done away with. We say in our brief that it may well have created interests which it would be unfortunate to disturb -- they have relied on it -- but we do attack the principle, and we ask in the brief that the whole matter of subsidies should be treated as something to be avoided. Certainly a transportation subsidy we feel is the wrong way to go about it.

THE CHAIRMAN: Would that apply also to the feed grain freight---

MR EVANS: Well, it applies in principle to everything that involves transportation---

THE CHAIRMAN: You think those various things were mistakes, then, that other measures ought to have been taken?

MR EVANS: With respect, I would say so. With respect to those who thought otherwise, I think they chose perhaps what might have been an easy method of providing relief they thought should be granted, and I am not suggesting that the relief ought not to have been granted in some form, because I have not made a study of those things.

THE CHAIRMAN: You do not say what form the relief ought to have taken?

MR EVANS: We do in our brief. We do not say what form it should have taken in those cases, but I think

you could apply the principle we argue for.

THE CHAIRMAN: It is the cases, you see, that raise the questions.

MR EVANS: Well, sir, for instance, we will say what we think the principle ought to be, and if it was a mistake to have done what was done, then I suppose it follows that it should have been done the way we said in the first place.

THE CHAIRMAN: In that case, then, you must have in mind a principle which would be applicable to all cases.

MR EVANS: Yes, sir; although we do not ask that those interests which have benefited from the Maritime Freight Rates Act be disturbed by having that Act removed today.

THE CHAIRMAN: No; I understand. You seem to indicate that there have now been created certain vested interests under that Act.

MR EVANS: Yes.

THE CHAIRMAN: And you would not disturb them without careful study. All right, then; perhaps we can get your principles.

COMMISSIONER INNIS: With regard to paragraph 32, Mr. Evans, would it be fair to interpret your position by saying that you would not agree to the substitution of the words "to the advantage" for "at the cost"?

MR EVANS: I am sorry -- paragraph 32?

COMMISSIONER INNIS: Supposing you read:

"Further, if it is decided that any industry or any part of Canada is to be assisted at the cost . . ."

MR EVANS: Oh, yes, I see.

COMMISSIONER INNIS: I was wondering whether your view was so strongly entrenched that you would resent the suggestion that it might be assisted to the advantage of

the whole nation.

MR EVANS: I would like to think about that. Of course, I would not resent the suggestion, sir. " . . . is to be assisted to the advantage of the whole nation . . ." -- well, I am not sure of the implications of that. Of course, it must be assumed that if you are going to assist an industry at the cost of the whole nation, there must be some advantage to the whole nation in doing that; otherwise you have got a pretty difficult bargain for the taxpayer. But I do not know how far I could---

COMMISSIONER INNIS: Well, you do concur in the general view that there is the possibility of advantage; you do not rule out subsidies entirely.

MR EVANS: No; I think this must be said: For example, our position in connection with the grain rates is this, that if the producer of grain in difficult times needs assistance, we recognize that there may have to be some assistance given, and I assume that it must be considered that it is to the advantage of the nation to give it, otherwise it would not be given; but whether the words are interchangeable in that context, I would like to give some consideration to that.

COMMISSIONER INNIS: The Chairman was suggesting a reference to the Feed Grains Assistance Act; how would you regard that?

MR EVANS: Well, if it became necessary to subsidize the farmer using feed grains, then we think that the way to do it is to subsidize the industry, and not pay part of his transportation costs.

COMMISSIONER INNIS: But you would be doubtful whether it is necessary?

MR EVANS: Well, I haven't any view on that at

all. I have no idea of it myself, and I do not know that our witnesses have expressed any view about it.

THE CHAIRMAN: Then does the principle to which you referred a moment ago mean this merely, that in such cases it is the industry that should be subsidized, and not the railway?

MR EVANS: Yes.

THE CHAIRMAN: That is the whole thing?

MR EVANS: Yes; and I think Mr. McDougall was going to express some views on that very subject.

THE CHAIRMAN: Yes, we have already heard it.

MR EVANS: May I go ahead?

THE CHAIRMAN: Yes.

MR EVANS: Q. Having heard read those sections of the Canadian Pacific brief dealing with the question of subsidies, what view have you to express to the Commission?

A. I am in full agreement with them, sir. The Commission will have noted that it is Provincial Administrations which have taken the lead in demanding subsidies to railway services, because of some alleged need of assistance to the people of those provinces. It seems to me that the important thing is that the authorities who see the need for these subsidies should, if the subsidies be granted, be given the responsibility of distributing them. If it be true that any part of Canada needs a subsidy from the rest of the nation, then surely the distribution of this subsidy should be left to those authorities which demand it.

Q. What do you say as to the distribution by a central authority of such subsidies?

A. I think it is particularly desirable that central authorities should not distribute them, because they are too far removed from the community which receives them. There is no more reason to subsidize the people of any part of Canada

in respect of transportation than in respect of any of their other costs.

THE CHAIRMAN: Q. Pardon me. Where should the money come from? The Parliament of Canada?

A. Well, if you make a national decision it is bound to come from the Parliament of Canada.

Q. But then the Government of Canada should not have anything to do with its distribution?

A. Yes; on the ground that the closer you get to the grass roots---

Q. I beg your pardon? A. On the ground that the closer you get to the grass roots, the more economically the job of distribution will be done.

(Page 17788 follows)

Q. Well, would you have the Provincial Governments spend the money voted by Parliament?

A. Yes, I think so.

COMMISSIONER ANGUS: Q. When you say subsidies should be given to the industry, are you including or excluding the possibility of its being regional?

A. I was considering the position of regional industry, yes.

Q. For example, a subsidy to potato growing in one province, but not potato growing in another?

A. Yes, I think so. After all we reach closely enough to that condition now to make one, yes....If this is one way in which you are attempting to help a region, it is help to a region that I am thinking of, not help to potato growers as such.

Q. Well, politically is it not a little easier to defend transportation subsidy than it is to defend a regional industry subsidy?

A. I don't know whether it is easier to defend....is it not simply that it is a little bit easier to distribute? In logic I think it is always easy to defend; but if you hitch the giving of a subsidy to something that seems to be relatively fixed objectively, you can get away with it a bit easier.

Q. Have you anything in that connection to say about whether that kind of subsidy is more or less likely to become permanent, having regard to Dr. Angus's point? Is there anything in that?

A. Yes, I think there is; just because the railways are big, and because one of them can turn eventually to the

Government people feel that if they once get their hooks into it they need never take them out.

MR. MacPHERSON: Q. It would work both ways?

A. No, I don't think so, provided that the Board of Transport Commissioners - -

Q. Some of us think it works both ways.

MR. EVANS: Q. You were saying that there was no more reason to subsidize the people in any part of Canada in respect of transportation than in respect of any other of their costs. Have you anything further to say as to why there should not be a transport subsidy?

A. Yes, I do, sir, I do think that transport costs have not risen in step with other costs, and there is every reason to believe that subsidies if paid should not be in respect of transport.

Q. What do you say as to the Board of Transport Commissioners being the medium of distribution in a transport subsidy?

A. I don't think it is a suitable body to distribute subsidies. That body would be charged with this duty under many of the suggestions offered to this Commission. Nor should the railways be compelled to assume that responsibility, for it would bring with it charges that they were favouring particular industries. Subsidies are bad per se, but they are less offensive when they are distributed by local authorities.

COMMISSIONER ANGUS: Are you considering the Board's distribution of subsidies to industry, or the distribution of transport subsidies?

A. Distribution of transport subsidies, which is, I take it, what has in fact happened under the Maritime

Freight Rates Act. They certified a normal rate, and then the shipper pays less than that.

Q. Well, do you consider that by certifying the normal rate the Board is distributing a subsidy, or that it was simply carrying out the duty of a measurement in accordance with which subsidy is being distributed; that it is giving effect to government policy rather than to making a policy?

A. But with every passage of time it becomes less and less an objective measurement, and more a problem of policy.

Q. The normal rate?

A. Yes, sir.

Q. Could you illustrate?

A. What was the normal rate of June 30, 1927, was an objective fact; it was charged and it was paid. But when you come to say what should be regarded as a normal rate at June 30, 1950, you are just twenty three years away from your last solid base where charges were made and people paid.

Q. Do you mean when the Board fixes the normal rate it actually hears evidence about industries and their needs?

A. I don't believe so.

Q. Well, in that case is the distribution of subsidy in accordance with those things?

A. I was wanting only to say that it became a more and more rarified and theoretical calculation, as you move away from the base where the normal rate was the rate actually paid by the shipper.

THE CHAIRMAN:Q.You mentioned a while ago that

subsidies are distributed more efficiently and properly when done locally?

A. Yes.

Q. Have you any instances of that in the past history of subsidies?

A. Well, not - -

Q. I am talking of subsidies voted by the Parliament of Canada.

A. Not as to subsidies, although the nearest parallel I can find is in the use of relief funds in the 30's: that the closer you got to the grass roots, the more intelligently was the money distributed. I can point to particular rural municipalities in which there were no relief payments just because you had a particularly effective - I have forgotten the name of the Township officer - who would see to it that nobody was gravely hurt, but equally that people were not sitting around building up relief claims in lieu of work.

COMMISSIONER INNIS: Q. Was there not very close supervision by the Federal Government over expenditures even under those conditions?

A. I am not denying they did perhaps; I am merely saying that if municipalities did not actively co-operate a great deal slipped through the screens.

Q. It seems to me that you are rather supporting a violation of what is fundamental practice, that the power that controls the purse, which controls the collecting of taxes, should control expenditures?

A. If you want to say that I do not like subsidies, and therefore would like to keep it to the absolute minimum, yes, you are quite right - I don't.

THE CHAIRMAN: Go on, please.

MR. EVANS: Q. I would like to read from Part I of the Brief, at page 55, the paragraph beginning "Incidence of Freight Charges".

"The Commission will have noted the frequent statements from various sections and interests that each of them pays all the freight on everything bought and everything sold. Canadian Pacific urges that there should be wise counsel given to the nation on this point; that it should be made clear that this statement is true of no one; that the incidence of freight charges is on the economy as a whole; that it is totally impossible to draw lines on the map, or to establish distinctions between groups or individuals, and to assert that this area, that group, or a certain type of individual is more burdened by transportation costs than is some other."

Mr. McDougall, do you think it is impossible to say that any particular occupational group, or any particular area, pays the transport charges on what it buys and on what it sells?

A. No, I cannot accept that. Transportation is one of the costs of production. In the long run, it is borne by the consumers. That should be obvious. The price at which anyone buys anything includes all the cost of producing it, unless it be produced at an actual loss, which certainly cannot go on for long.

Q. How about the short run?

A. In the short run, when demand is strong, then the

whole cost of production will be passed on by the producer to the consumer. If, however, the demand is weak, the producer may not feel able to do this; but, in such circumstances the price which he obtains will be set by general market conditions, and a reduction in transportation charges will not be left in his hands. The trouble will be one of the difference between prices which the market will pay and total cost of production, not particularly in transportation costs.

The community as a whole bears transportation charges. In 1947, the latest year for which full statistics are available, gross freight and switching revenues of all railways amounted to about 4.5% of gross national product. This is much too small a share in the total to be an important factor in economic conditions, as some evidence to the Commission would suggest. It may also be suggested that it is much too small to provide a base for subsidizing other and larger sectors of the national economy.

Q. Now, in particular what would you say about the statement that farmers pay all the freight on what they produce and on what they consume?

A. It is a very doubtful statement indeed, sir. I hesitate to say so, but I think it tells a good deal about the state of mind of those who make it - -

THE CHAIRMAN: Q. It tells you what?

A. It tells a good deal more about the state of mind of those who make it than it does about the facts. I think it really has no place in economic discussion. A farmer in British Columbia who sells apples cannot pay the freight if the farmer in Saskatchewan who buys them also pays it. Farmers are not a known and identifiable class

of people who will pay more in a store than you or I will pay. A large percentage of all the goods which farmers buy is purchased by them in communities in which they are simply so many members of that community, and this tendency for farmers to buy where other people buy grows as motor transportation and other forms of travel increase. Transportation costs are paid by the country as a whole and collected in the prices which consumers pay.

MR. EVANS: Q. Do you think these claims are fair or otherwise?

A. Why, sir, my sense of fairness is offended by some of the claims. Most of these claims are made by people who till rich soil. I suppose there are few areas in Canada so well served by railways and highways as is the territory north of Kingston, where I live. It is mid-way between Toronto and Montreal, and therefore is near what are regarded as the best markets in Canada. It has been settled for a century and more. Yet, none of it is prosperous, and some of it is on the edge of poverty, because the soil is thin and poor. The fact that the farmers there are located in the very centre of Canada does not make them rich; and if subsidies are to be paid to farmers on good soil, who are at some transport disadvantages then some part of that subsidy will have to be paid out of their poverty by the farmers north of Kingston.

Q. What about the suggestion that farmers live a distance from their markets....?

A. Well, it is true they are at a distance, but it is also true of a great many others, who buy ^{their} goods and supply them ^{with} services.....It is one of the inevitable consequences of regional specialization.

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Q. Now, I want to turn to another subject, Mr. McDougall. What is your view as to the use of the cost of service principle as the basis of rate making in this country?

A. Well, I don't think, sir, that it is an acceptable basis.

THE CHAIRMAN: Q. You do not think so?

A. I do not believe it is an acceptable basis. I know of no place where the attempt to make rates solely upon this basis has ever been made. It was discussed as early as a century ago, and discarded.

MR. EVANS: Q. Have you any reference there?

A. Yes, there was an English Committee on railways; the year has slipped my mind....A House of Commons Committee.

Q. What do you gather from the failure to give effect to that?

A. The fact that the nearer one comes to applying it the more obvious would the disadvantages appear. I don't think it is possible to apply it with benefit in any economy. I know that railways in new countries like Canada could not have been built as early as they were if they had been compelled to make their rates upon a purely cost basis. I feel confident that the railway network which was finally established would have been much more restricted in its extent if the individual rates were based solely upon cost. I cannot think that this country would put up with such stringent limitation on development of new areas as that would involve.

Q. What would you give as your most important reason for that view?

A. Well, I think the most important reason is that goods vary greatly in their demand for transport.

The demand for transport on goods of high value is likely to be such that no rate increase which has been suggested would be likely to change the volume of movements, because of the relatively small proportion of the selling price of those goods that is represented by cost of transport. The demand for transport for low value goods is such that any increase in the cost of transport then may easily reduce the movement to a mere trickle because of the relatively large proportion of the selling price of these goods that is represented by cost of transport.

Q. Do you regard the high rate on high value goods as merely subsidizing the movement of low value goods?

A. No, I think the situation may well be the reverse; because it is true that the high value goods are going to move anyhow, that cannot be so. The low value goods moving at lower rates may not make an equal contribution per ton or per ton mile to the overhead, but they can make some contribution, and one that would be lost entirely if the traffic dried up because pure average cost rates were instituted.

In that situation the high value goods would alone bear the overhead costs, and their rates would therefore be higher, not lower, as a result of lower rated goods not being carried. It should be particularly remembered that the movement of low value goods is a basic factor

in the economy of the nation, and any policy which would inhibit or reduce the movement would inevitably disturb the demand for and the movement of high value goods. There can be little doubt that ^{the}cost of service principle would have a serious affect upon many established industries in Canada.

Q. Have you any particular example in mind?

A. Yes. I think the Commission will remember the stove manufacturers from Sackville, N.B., who were making stoves, and who used materials which were brought in from Ontario points, and whose major markets lay west of Montreal. If they were charged the full average cost on incoming and outgoing freight, they would probably lose a large part of their present market. Now, businesses of that kind are, in their aggregate, important. And they only continue to exist because the rate structure is not rigidly tied to cost.

Q. Mr. Brown, a witness for British Columbia, gave evidence in support of the cost of service principle. He dealt with it first as a principle, and then suggested some mathematical and statistical proof of his theory. Now, I would like to ask you first to comment upon the generalities of Mr. Brown's evidence.

A. Well, as I understood the suggestion of British Columbia, it was that the rate should be based more nearly on the cost of service principle; at the same time, the value of services principle was condemned on the ground that the function of the regulatory tribunal, in measuring reasonableness of rates under that principle is purely subjective.

He apparently thought, therefore, that since the cost of service principle was concerned only with the cost of providing the service, an objective test was readily provided for the regulatory tribunal by which to measure the reasonableness of rates.

This would seem to suggest that what Mr. Brown is advocating is not merely that the rates should be fixed more nearly on cost of service principle, but that they

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should be fixed absolutely on a cost of service basis.

Q. Do you hold any opinion as to the way in which the value of service principle could be applied?

A. Well, if the value of service principle is correctly applied it will assure that each commodity, or group of commodities, will bear the average variable cost attributable to their movement. It follows that if Mr. Brown were right in his view that the costs which are variable with traffic are a substantially higher proportion of total cost than has been considered to be the case, the value of service principle need not be abandoned to reflect this condition.

Q. What does it mean then?

A. It only means that the minimum rate which is compensatory must be higher than people formerly thought.

Q. Have you any general comment on Mr. Brown's condemnation of the value of service principle?

A. Yes, sir. If I interpreted him correctly, he must either condemn the value of service principle outright in favour of the adoption of the cost of service principle, or he must admit that the value of service principle is sound.

Q. I gather from that, that you say there is no half way between those two?

A. No, I believe there is not.

Q. Other than so far as the cost of service is represented in the value of service principle?

A. Yes.

Q. How does the element of cost enter into the value of service principle?

A. Well, under the value of service principle the

1. The first part of the paper is devoted to a general discussion of the problem of the origin of life.

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18. The eighteenth part is devoted to a study of the various theories of the development of the human will.

19. The nineteenth part is devoted to a study of the various theories of the origin of the human emotions.

20. The twentieth part is devoted to a study of the various theories of the development of the human emotions.

21. The twenty-first part is devoted to a study of the various theories of the origin of the human passions.

22. The twenty-second part is devoted to a study of the various theories of the development of the human passions.

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26. The twenty-sixth part is devoted to a study of the various theories of the development of the human vices.

27. The twenty-seventh part is devoted to a study of the various theories of the origin of the human sins.

28. The twenty-eighth part is devoted to a study of the various theories of the development of the human sins.

29. The twenty-ninth part is devoted to a study of the various theories of the origin of the human crimes.

30. The thirtieth part is devoted to a study of the various theories of the development of the human crimes.

element of cost which is primary is the out-of-pocket cost, which is in reality the average variable cost, thus, provide a floor below which the rate fixed on the value of service principle must not go.

Q. Now, is there another element of cost in the value of service principle?

A. Yes. Under the value of service principle the maximum rate of return allowed by the regulatory tribunal to the railway providing the service must not be exceeded; and this, in effect, sets the upper limit beyond which levels in total resulting from rates fixed under the value of service principle may not go.

Now, in the area between that lower limit, the out-of-pocket cost, and the upper limit fixed by the total permissible rate, the value of service is the only practicable guide. In applying it all the advantages obtained by using the cost of service principle will be gained to give the necessary flexibility.

Q. The suggestion seems to be made that there can be some kind of combination, or as Mr. Brown put it, more nearly on the cost of service principle. Have you anything further to say about that?

A. The cost of service must provide the floor below which the rate cannot go; and actually, the cost of service is a factor in establishing the total rate to come into consideration where the maximum rates are being considered.

The total cost of service, therefore, always remains the ultimate limit in establishing rates; but the value of service is the working principle which sets the rates on individual commodities within those limitations. It is desirable to ^{use} both, in the interests of the

user of the railway service because of its flexibility, and in the interests of the railways because it is only by the use of this principle that the railways can hope to obtain adequate revenues where they can be found.

Q. Would you comment, or give us your view, as to such a major change from the present system, and what the effect would be on the economy?

A. Well, the whole economy has been built up on a rate system based on the value of service principle, and I would expect that any major alteration in it would involve a very major reorientation of the economy.

Now, I do not think it is possible to fully visualize the degree of disturbance, nor the duration of such movement, but it seems reasonable to say that no matter what the estimated benefits might be - - and for myself I think they would be negative rather than positive, they would not be sufficient to compensate for the dislocation involved in the change-over. In the result the so-called cure would be worse than the alleged disease.

COMMISSIONER INNIS: Q. You make a distinction then between what one might call the Canadian Pacific cost of service and the British Columbia cost of service? You seem to be using the same term to cover two different things?

A. If I understood Mr. Brown, he started off with the cost of service on the ground that there were no fixed costs, that all costs were variable, and therefore there was no basis for a spread of rates beyond those that were justified by difference in loading characteristics. Now, what I am saying is this - but first, perhaps I should say that I just do not believe that his statistics tell him what he thinks they tell him

about the absence of constant cost...But leaving that one aside for the moment. Once you talk about moving more nearly to the value of service principle - - rather, more nearly to the cost of service basis - - then I think you are in fact dragging in by the back door what you threw out the front. You are really taking the cost of service, which is the minimum under the value of service principle, and then trying to work out something beyond that. I think there is an inherent contradiction in his position.

Q. I am just wondering whether you are using the words in the same sense; whether logically you should not abandon the words "cost of service" in your general interpretation. I don't think that is what the British Columbia people mean.

MR. EVANS: I am not sure that I follow what you have in mind, Dr. Innis.

COMMISSIONER INNIS: Well, as far as I understand it, the British Columbia Brief was that the cost of service is something that can be worked out.

Q. And now, as I infer it, you think the cost of service is something which can also be worked out, but for a different purpose?

A. Oh, I think you can be quite clear, or reasonably clear, about what your out-of-pocket costs are.

Q. Wouldn't it be less confusing to abandon the words "cost of service " from the standpoint of your interpretation?

A. Well, if you will suggest an acceptable term I will adopt it. I think that is my difficulty.

Q. Well, out-of-pocket or allocable costs.

MR EVANS: I think perhaps what Dr. Innis has in his mind is that cost of service is either the full cost or it is not an in part cost. Cost of service embraces everything; is that what you---

COMMISSIONER INNIS: Well, I am thinking of the British Columbia position as I understand it.

MR EVANS: Well, if the is any confusion in this terminology, does it help to say this, that the cost of service is an element in the value of service? Now, it does not follow that you follow, as British Columbia does, the idea of having your rates reflect only the cost of service. Does that create confusion in your mind?

COMMISSIONER INNIS: Well, I think if you use the word "cost of service" you to some extent concede British Columbia's position. Here is something which apparently has content, it is something which is worked out to its logical conclusion, whereas the way in which it is being used would suggest that it ought not to be referred to as such at all, it ought to be referred to as simply allocable costs or out-of-pocket costs or whatever you like.

THE WITNESS: Well, would it meet your difficulty if we took those average variable costs on the one hand and all-in costs on the other?

COMMISSIONER INNIS: Well, I don't know that it is my difficulty so much as it is yours.

MR EVANS: If you are in any difficulty as to our view, and our friends of British Columbia have any idea that we have admitted the validity of their case, because we use that term "cost of service", I can tell my friends that we do not. I am sorry I have not made that clearer.

Q. Now, you have been talking about this question of principle; have you any observation to make about the difficulties of putting it into effect, say from the standpoint of accounting costs and so on?

A. Yes. I think that the accounting cost is a minor but still an important factor, because once you try to find in your accounting system the separate costs of particular shipments, or even of separate classes of traffic, you are going to run into something that is going to be impossibly expensive. In all the countries of which I have been able to find record the available cost data are those of performing particular functions -- the maintenance of way and structures, maintenance of equipment, conducting transportation, and so on. These have to be kept in any case for the information and use of the railway officers in controlling their money outlays, and any separate cost analysis attached to particular types of traffic would have to be in addition and would have to be far more detailed in order to be of any use whatever. And, furthermore, no matter how much money you spend on assembling costs, their application to any particular small part of total traffic is bound to involve a substantial element of arbitrariness. It will not give certainty, it will merely provide a numerical answer, provided certain assumptions are accepted.

Q. Now would you like to summarize what you have been saying up to date on this question?

A. Yes. What I have been saying is that any attempt to fix rates on the cost-of-service basis would end in an addition to railway expenditures and in a system of rates which might disrupt the whole economy of the nation, by stopping the movement of many sorts of low-value goods, greatly reducing railway revenues, and quite possibly

forcing rates on high-value goods up to a prohibitive point.

Q. What would be the result of stopping the movement of low-value goods, in your view?

A. Well, if you stop the movement of low-value goods you put out of work the men who produce them, and therefore their capacity to buy high-value goods.

Q. Perhaps I should not have said stop it altogether, but what I meant was that in principle you say that to the extent that you do inhibit the movement of low-value goods you also inhibit the consumption of high-value goods?

A. Quite.

Q. Now, I gather from what you have said that you condemn the cost-of-service principle as---

A. As a primary basis to organize a rate structure, yes, sir. The problem which faces the railways is the problem of getting enough money to cover the cost of their services. Every merchant has the problem of getting what he can where he can. Every merchant sells some goods on a lower percentage of spread than he sells other goods, and in the end no merchant, no manufacturer, no professional man -- I might say no one doing business of any kind -- makes the fixing of his prices on the cost of goods or services a rigid principle. Everyone knows that he can only charge what the traffic will bear. I have never heard of a doctor, or for that matter of a lawyer, who did not give some consideration to the financial position of his clients in deciding what charges to make. I think they all try to obtain a sort of basic rate, but they vary it up and down as circumstances require.

MR SHEPARD: Q. What about economists?

A. They are invariably modest, Mr. Shepard.

MR EVANS: Q. Now, what principle do you think lies behind what you have been saying?

A. I think there is a very great principle, and I would like to try to state it clearly. Railways exist to serve the transportation needs of the nation and not to serve as a laboratory for the testing of doctrinaire economic theories. Because they are a strategic sector of the national economy, the nation as a whole has the most urgent reasons for seeing that they remain in economic health; for if they fail to serve effectively the whole nation suffers. They are like the rest of us, they are just poor fellows trying to get along, and, like the rest of us, they have to be pretty free to adjust their charges to what the traffic will bear or they will not get along; and, since their getting along is of the most fundamental interest to the nation, it should be the first principle of rate-making that they be allowed to use a flexible principle of charging based on demand in order to get enough revenues to permit them to operate.

Q. Does this suggest to you that the railways are indifferent to matters of cost?

A. No, sir, I do not think they are. If they actually were indifferent to questions of cost, then they ought to change their traffic officers. The cost of service, that is, the over-all cost of service, represents what the railways must have in order to continue to operate. Their financial results, and particularly in recent years, indicate that they are not really too successful in meeting over-all cost. So that I feel that it is important to give them the greatest amount of freedom which is consistent with the law against discrimination.

Q. Now, Mr. Brown's evidence also dealt with some statistical material and calculations, and at page 100 of Part II of the Canadian Pacific brief that subject is dealt with in answer to Mr. Brown. That goes on for four or five

pages. I am not going to read those to you, but I would suggest to you that at that part of our brief the Canadian Pacific is rather critical of the approach made by Mr. Brown in his attempt to prove that costs are substantially one hundred per cent variable with traffic. Are you---

THE CHAIRMAN: We will rise for a few minutes now.

(Recess)

MR EVANS: Q. At the adjournment, Mr. McDougall, I had been about to ask you about the procedure adopted by Mr. Brown in his evidence to support his theory, and I had referred to the pages in the brief which criticize that, and I was going to ask you whether you agree or disagree with the criticism contained in the Canadian Pacific brief?

A. I agree with it, sir, yes.

Q. Well, did you hear the evidence of Mr. Brown in February, the 9th and 10th I think it was, and have you given consideration to the further arguments he then offered in support of his position?

A. Yes, sir, I have.

Q. At pages 14773 to 14775 in the transcript Mr. Brown seemed unable to accept a return on capital, net after income tax, as one of the costs of operation; what do you say about that?

A. Well, sir, I cannot agree with it. The nearest I can come to defining his position is to say that he wants to restrict the term "cost" to describe what railway accountants call railway operating expenses.

THE CHAIRMAN: Q. Railway what?

A. Railway operating expenses. Now, that seems to me to be a sterile distinction. In logic the cost of anything which is in the long run necessary to the provision of a

service is a cost of that service. In an expanding society additional capital is necessary to railways, which must correspondingly expand and improve their services to meet the demands of a growing national economy. Now, I know of no way in which private railways can get control of capital except by offering payment for its use. If corporate income tax makes a larger gross income necessary in order to be left with an adequate net income, then corporate income tax is equally a cost of production. Both the net return and the income tax which has to be paid before there is a net at the disposition of the corporation are necessary costs of providing railway service.

Anybody can split hairs on terminology, but if the word cost is to be given the restricted meaning which Mr. Brown proposes, then some other word must be found to express that wider meaning of the full cost necessary to the provision of service. It seems to me much better to leave the word expenses as meaning railway operating expenses as they are now defined, and to use the word cost as covering the all-in costs including income tax and the net return upon the capital used. It seems to me that Mr. Brown himself recognizes the logical necessity of covering the all-in costs in the following words, which are at page 14774:

"First, with regard to the question of including income tax as a cost, it may be true that in making a rate award, a regulating body might take into consideration the amount of income tax that a corporation would be subject to, and I understand that this is usually done."

To refuse a return upon the capital is to assume that the property is to shrink and its present owners are to be forced into bankruptcy. Now, I know of no serious

student who does not recognize that railways are the lowest cost agency of land transport, which must not only be maintained but must be expensed with the growth of the economy.

Q. At page 14784 of the transcript the following statement was made by Mr. Brown:

"Furthermore I can see nothing wrong with the single index per se."

He had been there talking about the criticism made in the Canadian Pacific brief, that he had used a single index in his studies. Then he goes on:

"It is not very enlightening to compare the index we prepared with those to which reference has been made by the Canadian Pacific, which were designed for use in a different type of analysis."

Now, do you agree with him, that the Interstate Commerce Commission index or indices were "designed for use in a different type of analysis"?

A. No, sir I do not. The two analyses were made for an identical purpose, namely, to see how rail costs varied with the volume of business done. The differences are differences in the approach to the problem, not in the purpose. Mr. Brown confined his attention to a part only of the total cost, namely, the railway operating expenses, whereas the Interstate Commerce Commission study took "freight operating expenses, rents and taxes", so that it explicitly recognizes the existence of capital costs.

Secondly, it seems to me that Mr. Brown is something less than candid in reporting the results of the Interstate Commerce Commission study when he says:

"The more surprising end, shall I say, vindicating thing is the fact that the end results were so nearly alike, that is, the result of this study and of our own

were nearly alike. We dealt with aggregates and they dealt with components."

MR EVANS: That will be found on the same page, my lord, page 14784, that the witness has quoted.

Q. Now, I gather that he is arguing there that fixed costs are negligible?

A. Yes, sir, he is. Now, the Interstate Commerce Commission study shows for the year 1946 the fixed costs of the western lines of the United States are over 20 per cent of total costs. I say flatly, they do not confirm Mr. Brown's study. If anything, the Interstate Commerce Commission study makes his conclusions inherently improbable.

I should add that the United States western lines are nearest to the railways of Canada of all the sections of the United States in their average density and in their general operating conditions.

Q. Now, on the same page and over on the top of the next page Mr. Brown was dealing with the question of weights used in his index, and he suggested that his use of average weights for the whole period minimizes, as he calls it, the bias which he says is introduced into the index by the use of an index number. What have you to say about that?

A. Well, he used the average of the whole period, and he says it is better than to base it on either the beginning of the period or on the end of the period. Now, he is quite right in that, but it still does not absolve him from the charge of making a shotgun adjustment by applying a single price index to the reported total operating expenses. Any single index of this kind assumes that the relative weights of the several classes of expense remain approximately constant in relation to

each other over the whole period. Now, this is clearly not so. It is not even necessary to go to the Statistics of Steam Railways to prove that it is not so. The Canada Year Book, for example, shows that wages as a percentage of total operating expenses amounted to 66.1 per cent at 1930, to only 52.5 per cent at 1943. Traffic expenses amounted to 5.2 per cent of total expenses at 1932, to only 1.7 per cent at 1945. Therefore what purports to be an adjusted series of expenses is in fact too crude to be a dependable base for any further analysis. Now, how great the errors are can only be determined by duplicating the I.C.C. study using Canadian data, or at least by correcting each of the five major sets of functional accounts by a price index which is directly applicable to it.

Q. Do I understand you to say that his deflated operating costs are too crude -- is that the word you used -- to be the basis of any further analysis?

A. Yes, sir, that is it exactly. The changes in the volume of business and in prices over the period are so wide that I do not think his basic series of deflated operating expenses is a dependable series.

Q. Now, the Canadian Pacific brief also is rather critical of his use of the unadjusted figure of locomotive miles; would you like to comment on that?

A. Yes. There were progressive changes in the average size and tractive power of locomotives over this whole period, and therefore you have a progressive distortion of the results. If a locomotive mile represents one unit of input of effort at 1923, as Mr. Brown suggests at the bottom of page 14790, then by 1937 it represents 1.9 units.

Q. Is that 1.9?

A. 1.19 units; and by 1947 it represents 1.28 units. The fact that this change is progressive gives Mr. Brown the

smooth lines of relationship which he finds, but as time goes on he is comparing unlike things.

Q. Now, at pages 14794 to 14800 Mr. Brown advances the argument that his charts 3 and 4 support his contention that deflated costs vary directly with traffic. Do you accept that argument?

A. No, sir, I cannot. I think there are two grave breaks in that argument. First of all, his operative equations, which are given at tables 9, 9A and 10, and whose results are in charts 1 and 2, deal with total locomotive miles, whereas charts 3 and 4 deal with freight locomotive miles only. If there is a difference between the cost per freight locomotive mile and per passenger locomotive mile, and if the proportions between the respective mileages are changing, and they did so change, especially in the period 1938 to 1947, then that demonstration is left in mid-air.

Q. Anything else?

A. Well, at page 14801 of the transcript Mr. Brown repeats what was said at page 9 of his original submission of June 22nd, namely, that the reported expenditure of any one year need not be the actual cost of giving service in that year. Now, if in fact the maintenance outlays are to a substantial degree controlled by the amount of revenue, then it follows that the true relationship will certainly be different from the one Mr. Brown shows, and may actually be the curvilinear one which he expected (page 14803) and which he failed to find because of the defects in his method.

(Page 17821 follows)

Q. Now then, on the two following pages, on 14804 and 14805, Mr. Brown professed himself unable to understand a criticism of his work contained in the following words at page 102 of Part II of the C.P.R. brief which I am now going to read to you:

"Mr. Brown could have had an equally close fit of his data to a line of relationship in two quite different graphs; that is to say, the same relationship might have been obtained in one graph which would show that there were no costs which were constant and in another where as much as 99 per cent of costs were constant and only one per cent variable with traffic."

Can you give the Commission assistance in understanding that?

A. Yes, sir. In the British Columbia submission of 22 at page 14 the whole weight is thrown upon the close correlation between locomotive miles and the adjusted expenses. June

"The point that we wish to make is that when the disturbing element of a changing price level is removed there is a remarkably close correlation between the amount of work done in a given year and the expenses involved in doing that work."

And then, further down:

"One can only conclude therefore, that in the year to year results operating costs tend to fluctuate in close harmony with the amount of work done, and that any so-called constant element is of a relatively minor importance."

Q. Did he withdraw from the position as taken in the brief?

A No, sir. I have examined his testimony of February 9 and 10 rather carefully and I see in it no withdrawal from that position.

Since he relies upon the high coefficient of correlation he exposes himself completely to that criticism. I must repeat that the coefficient of correlation is in logic a proof of co-variation only.

What Canadian Pacific says is completely true, and it^{is} a non-sequitur in logic of the first order to suggest that Mr. Brown's equations prove that;

"any so-called constant element is of a relatively minor importance."

Q. On pages 14805 and 14806 of the transcript Mr. Brown suggests that his curves should not be extrapolated beyond the observed limits of the data and therefore that the Canadian Pacific comment at pages 102 and 103, repeated in the transcript at pages 14805 and 14806, is really irrelevant. What have you to say about that?

A Well, I willingly admit that the extrapolation gives a nonsensical result, but Mr. Brown should, nonetheless, have taken it seriously.

If he had confined himself to working with the deviations from the mean of the data, that is with an equation $y = bx$, he might have had an empirical curve of very limited usefulness, but usable within such limits.

But once he tries to derive estimates of the constant costs he is automatically using the curve in the form $Y = a \text{ plus } bx$ and is directing his whole attention to the factor "a" in that equation

which shows the constant costs.

All that Canadian Pacific has done in this statement is to highlight the fact that the results do not support the conclusion based on them.

Q. Now, you have given us some criticism of Mr. Brown's work in this connection. I suppose that is negative rather than positive criticism. How, in your opinion, should such a problem be approached positively?

A. It is a little bit difficult to follow, but I can try.

First of all, I think that you should not lump all your expenses together. You should vary each of the functional accounts separately, and thus, having corrected each functional account separately, to combine the result.

And secondly, I do not think that any gross correlation such as Mr. Brown used can possibly give a useful or dependable answer.

I think that at a minimum one needs at least three independent variables in a multiple correlation equation.

I have done some work in this field, work with transportation expenses, in which I found it necessary to use three independent variables, gross ton-miles in freight service, passenger train car-miles, and total train miles.

I also experimented with additional independent variables, and I found that when I brought in the total freight car miles, I had got a moderate net increase in accuracy, after allowing for the reduction of one degree of freedom. But for most purposes the equation with only three independent variables was adequate.

I should add that while this is useful in dealing with the transportation expenses, I have not yet found an approach on which I am willing to depend in analysing the maintenance expenses, because I have not yet come upon a logically water-tight method for separating out the effect of variations in revenue upon these accounts.

Q. Would you say that the problem is unsolvable?

A. No, I do not think it is insoluble. But if I were given a staff of two assistants, I could do the job; but I think I would want to have the full co-operation of the railways; and I would get an answer which was crude but usable, perhaps in 12 to 18 months.

Mr. Brown's work is really not of any help. I do not think it even provides a starting point.

Q. Why do you say that?

A. I say that because correlation, as I have said is a proof of co-variation only and not of causation.

Before any gross correlation such as Mr. Brown uses can be used with any confidence, it is necessary to have:

- (a) some logical ground for making a connection between the two variables; and
- (b) to have explored all the other possible correlations and to have proven that the one chosen does in fact give a closer fit than any of those which are rejected.

To light on one factor such as locomotive miles without making such a proof is a little beyond the pale.

Q. Now then, to turn to another subject, Mr.

McDougall, perhaps I might read to you four paragraphs from page 64.

THE CHAIRMAN: Of which volume?

MR. EVANS: From Part I, sir. These paragraphs are numbered paragraphs of the outline submission, and I read:

"42. Canadian Pacific submits that in order that rates be just and reasonable to the railways, the general level of rates should be such as to provide an equitable return on the investment in railway property used in transportation service.

43. The present jurisprudence in public utility regulation holds that historical book records of investment are the best evidence for establishing a rate base. The necessary data in regard to the investment of Canadian Pacific is available in the records of the Company. No need, therefore, exists for a prolonged and expensive investigation into the value of the property used in transportation service.

44. In establishing a fair rate of return, the matters to be considered include the need for raising new capital in the financial markets in competition with other seekers of capital. In 1948 the rate of return obtained by the Company on its depreciated book investment in railway property was 1.78 per cent, whereas studies have shown that the cost of capital employed in the railway enterprise at the end of 1948 was not less than 6.52 per cent. The serious handicap facing the Company in raising new capital under

present conditions is indicated by this comparison.

45. It is submitted that no amendment is necessary to the Railway Act of Canada to apply the principle of fixing general rate levels on the basis of a fair return on the investment in railway property used in transportation service. The determination of investment in such property and of the rate of return are matters which should properly be left to the Board of Transport Commissioners."

Now then, have you some views, Mr. McDougall, on that subject, which you would like to offer to the Commission?

THE WITNESS: Yes. I think there will be unanimous agreement, that, in the words of the Outline Submission,

"the general level of rates should be such as to provide an equitable return on the investment in the railway property used in transportation services."

Any difference of opinion must arise on the details and not on principle, over the rate of return which is to be considered equitable, or over the base of capital invested on which that rate of return must be calculated.

No enterprise can hope to raise additional capital, whether for the replacement of maturing issues, for necessary expansion of operations, or for any other reasons, except if its prior record of paying return is reasonably good.

MR. EVANS: Q. What significance do you attach to the use of the word "equitable"?

A. I think that "equitable" is primarily of physical significance.

THE CHAIRMAN: Q. Primarily of what?

A. Physical rather than economic.

For economic purposes, an equitable rate of return is one which will cause the market value of a capital investment which has been wisely and prudently made to be maintained at such a level that new capital can be obtained, to replace maturing issues or to provide for expansion on terms which will leave

1. The first thing I noticed when I stepped out of the car was the cold, crisp air. It was a relief after the warm, stuffy interior.

2. The second thing I noticed was the sound of the city. It was a mix of honking horns, car engines, and the distant chatter of people.

3. The third thing I noticed was the sight of the city. It was a vast, sprawling metropolis with tall buildings and a network of streets.

4. The fourth thing I noticed was the smell of the city. It was a mix of exhaust fumes, street food, and the general scent of a busy urban environment.

5. The fifth thing I noticed was the feeling of the city. It was a sense of being part of something big, something that was always moving and changing.

6. The sixth thing I noticed was the sight of the people. They were all going about their business, some in a hurry, some in a relaxed pace.

7. The seventh thing I noticed was the sound of the traffic. It was a constant hum, a backdrop to the city's life.

8. The eighth thing I noticed was the sight of the lights. They were everywhere, from the street lamps to the neon signs of the city.

9. The ninth thing I noticed was the feeling of the sun. It was a warm, golden glow that bathed the city in light.

10. The tenth thing I noticed was the sight of the clouds. They were soft and white, floating in the blue sky above the city.

11. The eleventh thing I noticed was the sound of the birds. They were chirping and singing, adding to the city's symphony.

12. The twelfth thing I noticed was the sight of the trees. They were green and leafy, providing a touch of nature in the urban landscape.

13. The thirteenth thing I noticed was the feeling of the wind. It was a gentle breeze that rustled the leaves of the trees.

14. The fourteenth thing I noticed was the sight of the water. It was a calm, reflective pool that mirrored the city above.

15. The fifteenth thing I noticed was the sound of the waves. They were crashing against the shore, creating a rhythmic pattern.

16. The sixteenth thing I noticed was the sight of the sky. It was a clear, bright blue that stretched out over the city.

17. The seventeenth thing I noticed was the feeling of the earth. It was a solid, stable ground that supported the city and its people.

the owners of the older securities and the buyers of new issues receiving a similar return on their actual investments.

Q. Do you consider that stock markets react automatically?

A. I am not making the argument on it, that it is to happen tomorrow morning. What I am really saying is that, since the setting up of a rate of return is something done upon an average, on the nearest you can come to a long-run normal, then you would have regard to what happened in that same long run to the market prices of the stock, yes, because ultimately you will be compelled to go to that market and to submit to its valuations, if you are going to get capital from it.

MR. EVANS: Q. Is what you have been saying related to the matter of the transfer of capital between security issues, or what we may call dilution of equities?

A. Yes, I think it is, because it is not proper to introduce new capital under conditions which will transfer to its providers part of the equity which has been built up by earlier investors.

That may or may not be good ethics. But the economist, I think, is compelled to say that any attempt to make such transfers as between capitalists is, in the end, self-defeating.

Q. When you speak of transfers and dilution, am I correct insaying that when you sell shares at, let us say, a substantial discount, it produces that result? Is that your view?

A. Yes. The argument I have runs in these terms: that where you have a security outstanding on which the full par value -- as well as the premium thereon and

upon which there have been substantial surpluses accumulated, if you then sell to new people at less than par, or if you sell at par, we transfer an interest in part of the surplus to them by the new shares.

COMMISSIONER ANGUS: Q. Does it follow from that that when you have the rail income alone, you think it should be sufficient to pay the dividends which would enable the stock to sell at par; and that with the addition of Other Income, it would therefore sell at a substantial premium?

A. It depends on whether the rail investment is alone equal to more than par. If that is so, then it follows. But if it were not so, it would not.

COMMISSIONER INNIS: Q. Have we any figures on the net?

MR. EVANS: I think there was a figure put on the record. I would be glad to look it up for you.

COMMISSIONER INNIS: But not over a period of years, as in the case of the railways?

MR. EVANS: No. Perhaps it is not an answer, but Exhibit 196, here 49-49, is where they divided the two halves of the balance sheet between rail and Other Income. I think you will find there the figure of investment in both, whether in gross or net, after deducting depreciation.

COMMISSIONER INNIS: Q. Is the interest rate worked out in the same way?

MR. EVANS: The interest rate on the securities?

COMMISSIONER INNIS: In Exhibit 190 I think the railways made for us a comparable figure?

MR. EVANS: No, what was done in that statement A, of Exhibit 196, was to allocate to rail

all the debt securities on the theory that that was the lowest return basis for the rail, and leaving a much lower equity capital in the rail than would otherwise be the case. There is a footnote there which was explained in the 20 per cent case saying that if it did otherwise than allocate the debt securities, the equity balance in rail would be higher, and should have a higher return on that account. Does that answer your question?

COMMISSIONER INNIS: Yes. I was only interested in getting some comparable table getting the interest rates on investments.

MR. EVANS: The only evidence we have in this case is that reported in the Exhibit which Mr. Liddy put in, and showing something over 3.8 per cent in 1948, with Other Income activities.

COMMISSIONER INNIS: Q. But you have not the Other Income activities?

MR. EVANS: We have got the figures of investments in Exhibit 196. Take in any given year the amount of Other Income. We can take the income in that year which is shown in the Exhibit and calculate the return. I would be glad to look at it and see what can be done. And if you would like a statement on that we will file it.

COMMISSIONER INNIS: Yes.

MR. MACPHERSON: I would be the first to argue that 49-49 was not accepted by the provinces.

MR. EVANS: I was not suggesting that the provinces accepted it. But I do not think the provinces disagreed with the actual figures in that statement.

MR. FRAWLEY: That Exhibit 196 only includes some of your Other Income.

MR. EVANS: We were not talking about that as a matter of income, on that Exhibit. I am surprised to hear you say that.

THE CHAIRMAN: What did Mr. Frawley say?

MR. EVANS: He said that Exhibit 196 which was put in in the 20 per cent case, and put in here, does not contain all the Other Income.

MR. FRAWLEY: You are speaking of 49-49?

MR. EVANS: Yes.

MR. FRAWLEY: Oh no, no.

MR. EVANS: You mean the one which listed the nine? The nine items of Other Income.

MR. EVANS: I was not suggesting --

MR. FRAWLEY: It starts with "communications".

MR. EVANS: What I was suggesting to Dr. Innis was that if you wanted to get a return on that Other Income investment, you would have to go ^{to} 49-49 for the investment; and then you would take the revenue for other income in the company's report in that year, and take off your income tax allowance, and then calculate your return.

THE CHAIRMAN: Does that column in your Exhibit 196, which is headed "Other Income" include everything?

MR. EVANS: Oh, no sir. If it included everything that would have been an easy way to answer.

MR. MACPHERSON: It does not include Consolidated Smelters at all.

THE CHAIRMAN: Then what does it include?

MR. EVANS: It includes merely those nine divisions.

THE CHAIRMAN: Upon which Mr. Liddy made his calculation?

MR. EVANS: I am sorry, sir.

THE CHAIRMAN: The nine enumerations upon which Mr. Liddy made his calculation.

MR. EVANS: I think your lordship referred to Exhibit 190, but it is Exhibit 189, to be correct.

COMMISSIONER ANGUS: In paragraph 44 which you read, Mr. Evans, mention was made of the figure 6.52 per cent as the cost of capital employed in the enterprise.

If you were considering the cost of new capital let us say, today, would the rate at which it could be raised depend substantially on whether or not the Board of Transport Commissioners had accepted these figures as to how the rates should be determined?

MR. EVANS: Well, I should say if they had not accepted them, that the investors were doubtful of the long-run prospects of the industry, that percentage would tend to increase rather than to decrease.

COMMISSIONER ANGUS: And if they did accept in a clear-cut way?

A. Then I would expect that the market price of the common stock would tend to discount the earnings prospect at a lower rate per cent, and therefore you would raise new capital more cheaply.

COMMISSIONER ANGUS: So, other things being equal, the level of surplus would be a bit lower than if one had -- if these figures were fixed?

MR. EVANS: Yes.

COMMISSIONER INNIS: Q. Let us assume

that your market conditions are always favourable for stock?

A. Not necessarily. It only assumes that you cannot continually increase your debt without coming very soon to the point where people reject the debt also.

Q. It seems to me you have quite a different problem if there is a market condition favourable for bonds which is followed by, say, a period which is favourable to stocks, and the company would have to operate in relation to the marketability of securities?

A. Well, naturally you would have certain limits within which you would want to vary the proportion between debt and equity. There might be a point below which you would not want to reduce your debt; and equally there is a point beyond which it is grossly unwise to increase it.

COMMISSIONER ANGUS: Q. But that point too would be affected by what the Board would do?

A. Quite, because the lower the expectation of earnings, the greater is the pressure on the company. It must expand to get money in some fashion or other.

Q.
MR. EVANS: / While we are still on that point, what experience have you, in general, of the way in which management handles this problem

of selecting markets, and having regard to the conditions under which they can make offerings?

A. Well, I have talked to some people who had to make that kind of arrangement in the last four years, and I have seen them in some cases sell preferred stock, even though they clearly faced a much heavier charge as a result of corporate income tax, just because

...and the ...

they were not sufficiently certain of their long-run prospects to take the risk of issuing debt securities.

Q. I was thinking more particularly of the conditions of the market at the time which seemed to be in Dr. Innis' mind?

A. I can think of some companies in which, having for a long period kept a very safe ratio between debts and stock, they have recently, under the pressure of a very great capital need, increased the proportion of debt. That is, they have sold both debt and stock. But the market conditions compel them to sell more debt than they would like.

Q. Yes.

A. I think you will find a very good example of what I am thinking of in the behaviour of American Telephone and Telegraph between 1914 and 1929.

Between 1914 and 1921 they were compelled by the state of the market to increase their debt proportion. But between 1921 and 1929, in the face of an average increase of about 7.5 to 8 per cent per annum in their assets, they sold so much stock that they cut their proportion of debt very sharply. I am almost urged to say by nearly one-half. They sold enough stock so that they financed all their increases in assets, and they held the debt practically stable, or reduced it.

Q. Yes.

COMMISSIONER AUGNS: I suppose these proposals involve making the Canadian Pacific its own yardstick?

A. Well, it is obvious that you cannot use the Canadian National as a measure. I do not know how else

you can do it except either to take it as its own yardstick, or to compare it with other regulated utilities, with allowance made for the variability of income from year to year.

Q. Do you think any United States railway is its own yardstick?

A. No. You have a hundred and thirty-one Class I railways there, and you can strike an average from them.

You cannot do that here.

Q I agree. But can you make a railway its own yardstick without impairing or even destroying the incentive which is supposed to matter so much in private enterprise?

A. I do not think it is in any sense a guarantee.
as
But insofar/there is any suspicion that they were lying back and leaning on the opportunity of increased rates, that ought to be investigated.

Q. You think then that it is a duty of the Board to conduct such an investigation?

A. I would think so; and I would feel happier in saying so just because the pressure of competition on other carriers removes a good deal of the weight of the problem from them.

THE CHAIRMAN: Q. Removes what?

A. Removes the weight of the problem from them.

COMMISSIONER ANGUS: Q. How?

A. When railways have substantially a monopoly of land transportation, then it is very hard to find something outside to compare with them. But when, for all their high-valued goods, they must face the trucks, and when there is a fringe of water-competition, then there are internal pressures on the railways themselves

to keep them up to scratch, which cannot have existed prior to 1910.

Q. As long as they have a monopoly on some transportation, would the effect of this prove to be to force that transportation, that share of the transportation that was subject to monopoly, to bear the full weight of bringing the earnings up to the required level, should they be impaired in other directions?

A. There would be a tendency in that direction, yes. But it seems to me that at the present time one of the reasons why the railways are not making a more rapid reduction in their costs is that their means are so restricted, that wholly certain and valuable savings from new capital investments are inhibited.

Q. Yes. But my question really has to do with this: would this theory remove their incentive to make reductions in their costs, or would it impair it?

A. Wisely administered, no. You mean "wisely administered" by the Board?

A. Yes, and I think by reason of the railways themselves, who would have a very great interest in moving their costs down as quickly as they possibly can in the face of the pressure with which they are faced; pressure on the Board that arises partly from the unequal treatment of today's means of transport, where some are actively promoted by the government, and others are regulated.

Q. But is it not a fact that these proposals would detract from the pressure of these competitive means of transport, because what you lose in competing in them, you can recoup from the monopoly scheme of your traffic, in theory at least?

A. There must be a limit to the amount to which you can go, a limit which the traffic department is constantly exploring, is it not? I should think they would probably say they are much more careful and more restrained in their exercise of that power than might seem at first sight to be their normal action.

Q. Well, would the situation be in any sense improved if you could have a Canadian National yardstick as well, if by some system, let us say, of handicapping, you could let other railways race against each other?

A. If you envisage a transfer of the Canadian National to private hands, I would think, yes; it would be a most interesting thing; because the Canadian National is, in many ways, a road with very great natural power.

Q. Why would the information be provided, if the capital structure is accomplished, or if the rate base is accomplished?

A. I think there are always pressures which are seen and unseen around the Canadian National which incline to make it pool its efforts in a particular direction.

Q. You do not think that the income tax is a sufficient handicap to balance against those pressures?

A. Well, it certainly is a countervailing force, but I question whether it is adequate.

Q. You think the Canadian Pacific should carry a little more weight?

A. Well, I would think you could; there are certain directions in which you can use Canadian National figures in a comparison with Canadian Pacific in, let us say, train-loadings, or something of that kind. But so long as the Canadian National can,

in the last resort, come to the government and say: We have a deficit. Then the restraint would, in many ways, relax on them; and secondly, the pressure to be self-supporting is denied to them. I do not think it is a matter in which fixed charges are important. I look on it more as a matter of operations.

THE CHAIRMAN: We shall adjourn now until this afternoon.

---At 1:00 p.m. the Commission adjourned until 2:45 today.

Ottawa, Ontario
Monday, March 13, 1950.

A F T E R N O O N S E S S I O N

PROFESSOR J. L. McDOUGALL - RECALLED

EXAMINATION BY MR. EVANS(Cont'd):

Q. I had a note on my book at the closing of this morning's session, Mr. McDougall, in connection with the question asked you by Dr. Angus as to whether there was any restraint on the railways faced with the situation that you described this morning of having competitive forms of transportation, with regard to the rates on the commodities that were not subject to competition and I was wondering if you had any views as to whether there might be a restraint to high rates in the principle that we have been discussing, the value of service principle?

A. Yes, sir, there is, that is, there is a general restriction in that limitation on the total earnings and in relation to the rates on particular commodities; you might very well run into a value of service restriction which would keep you in your earning power well below that accepted reasonable earning power. I suppose you might take the position of the 1930's in Canada as being an example of that kind of limitation, that in the face of a rather uncomfortable earning position you reduced rates rather than increase them on the ground that it was in that way that the community and the railways did better than they otherwise might have.

Q. Now then, to come back to the subject we were discussing before this later discussion arose, you had been saying that the economist took the view that transfers as between capitalists were self-defeating. Would you care to put your thoughts in that connection into somewhat different terms perhaps than you previously put them, by way of illustration?

A. Well, putting it positively, sir, I think a corporation has a right to seek a rate of return which will permit securities representing prudent investment to sell on the open market at their book value so that further additions to capital can be obtained without doing injustice to the original investors. It must be clear that, in order to arrive at this just treatment of the original investor a security issue which has a total par value exceeding actual investment need not sell at par. On the other hand, a security of which the total par value is considerably less than the total useful and prudent investment in the property should at all times sell considerably above par, and in order to do so the security must have a good record of a fair return to investors.

Q. What do you say about re-invested surplus earnings in that connection?

A. Well, earnings which are re-invested are capital put back into the business. They stand upon a par with the money subscribed for capital stock. They represent just as real an investment as that stock. A company such as the Canadian Pacific cannot be said to distribute an adequate return to shareholders because its common stock is presently selling on the open market at considerably less than par. This common stock represents an actual and useful investment considerably in excess of its total par value. You will understand, of course, my emphasis is not on the happening of any particular day but over a run of months or years as a minimum.

Q. Now then, would you discuss for a moment the question of the rate base and the total investment which should be considered by a regulatory authority in fixing a return on investment?

A. In economic terms I think that the genuine invest-

1. The first part of the paper is devoted to a general discussion of the problem.

2. In the second part, we shall consider the case of a single particle.

3. The third part is devoted to the case of a system of particles.

4. In the fourth part, we shall consider the case of a continuous medium.

5. The fifth part is devoted to the case of a system of continuous media.

6. In the sixth part, we shall consider the case of a system of particles and continuous media.

7. The seventh part is devoted to the case of a system of particles and continuous media.

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ment in an enterprise is the total cost of reproducing the property in equally useful shape less observed depreciation. For reasons with which the Commission is probably familiar in view of the general public discussions of the problem of providing for costs of replacements which have risen very rapidly in recent years, there has been established in the case of most regulatory tribunals the practice of using historical book records of investment as the proper base on which to establish rates. As the Canadian Pacific submission points out, it has proved difficult to find any other dependable method of establishing a rate base although various other plans have been suggested. However, the historical cost method of establishing a rate base does not, in my opinion, provide anything like an adequate rate base for the Canadian Pacific unless the rate of return is proportionately adjusted to the realities of the case.

Q. How would you consider a replacement cost base - -

THE CHAIRMAN: Consider what?

MR. EVANS: How would he consider a replacement cost base as against historical cost base?

THE WITNESS: I would think that at today's costs a railway property equal in capacity to that which the Canadian Pacific has built up would result in a rate base which is much higher than is represented by the depreciated book value of the existing property. The Canadian Pacific submission recommends use of depreciated book value as the only figure which can be practicably used as a rate base. My opinion is that, if this figure be used, then in order to obtain a true economic return there would have to be applied a higher rate of return on this value than if the present costs of reproduction less observed depreciation were treated as the rate base.

Q. You have spoken of practicability. What have you in mind about that?

A. I am thinking about the difficulty of making a physical measurement and evaluation of a whole property, and of the differences of opinion that appear in relation to inventory, to replacement costs, to observed depreciation, and so on. Therefore I look on the depreciated book value as the practical basis, at least under the present circumstances, and I suppose provided the price index does not go very much higher than it is now.

Q. What you say is as long as the return reflects the condition of which you speak?

A. Yes.

COMMISSIONER ANGUS: Q. When you say there should be a higher rate of return in that case, you mean a higher rate than is necessary to bring the stock to par?

A. Yes.

MR. EVANS: Q. I wonder if that is to be taken from that, Professor McDougall. Dr. Angus' question was when you spoke of a higher rate of return had you in mind a higher rate of return than was necessary to bring the stock to par, or a higher rate of return than would be necessary if you used a reproduction cost base?

A. Well, certainly if the net worth per share of ^{common} Canadian Pacific/stock upon a reproduction value is very much higher than what you want is the company on a rate base and rate of return which will allow your stock to sell in the market at something like that net book value on a reproduction basis.

COMMISSIONER ANGUS: Q. Then if you have on top of that earnings from other income it would merely mean the stock would be selling at what, two to three times what it is selling at today?

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A. Oh, probably, yes. I would think that the other earnings would in a sense provide the cream on the puff. They would be enough to let you sell your stock at about its replacement value, and that difference would be the spread that would lie between the current market value and the issue price under rights.

MR. EVANS: Q. Is that what is sometimes called market pressure at the time of issue?

A. Yes. That is, if your stock is selling at X you cannot offer shareholders the right to buy new shares at X and hope to have them taken up.

THE CHAIRMAN: Q. Hope to have what?

A. At X, any given value. If you hope to have the shareholders take up the new shares then you must offer them these new shares at something less than X.

COMMISSIONER ANGUS: Q. Of what order of magnitude would that difference be?

A. Well, Bell Telephone in the recent issue issued at 33 with the market around 42 and got away with it. I would think any narrower spread --

THE CHAIRMAN: Q. That is to shareholders?

A. Yes.

COMMISSIONER ANGUS: Q. Was that entirely to shareholders because nobody else would have bought, or were not rights given to shareholders that they could sell for something if they wished to, to others who wished to buy?

A. I would think it much more a matter of tempting in additional equity capital.

Q. But subscription rights sell for something?

A. Oh yes, but remember that what was paid to the man who sold was an interest in the surplus and general equity of the stockholder because the net equity was reduced after the new issue was made. It is a transfer as between

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the stranger because the old was

for the new was made. It is

investors; it is not a transfer from the company to investors.

Q. Perhaps not, but as I understand it, the man who buys the right to subscribe for the stock is paying for the stock at the price it is selling plus whatever he is paying for the right?

A. Yes.

Q. So that one is assuming that the price paid for the right is to some extent a measure of the estimate that the market puts on the security?

A. That is true, but except there is some kind of inducement nobody is going to give up cash which is capable of being put in any direction for this one specific direction unless there is some kind of inducement, and that right is the inducement. It is a cost of capital.

Q. What I am suggesting is that the difference between the price at which the stock is offered to the shareholder and the price at which it is selling in the market is rather more than is necessary to tempt subscriptions, and that the measure of its being more is what the rights will sell for?

A. Well, you have two options. The company can go to underwriters and have that issue underwritten for a fee, which is collected whether the underwriter takes up one share of stock or not, in which case you could narrow the spread, but if you are not going to use an underwriter then you have got to get that underwriter from the general market by widening the spread between current market and the issue prices, and I think on the whole it is useful for the Company so to do.

MR. EVANS: Q. Now then, you were discussing this need of an increased return if a historical cost base were to be used. Have you anything to add to what you said?

A. I think the point I am trying to make is that if a depreciated book value or a historical cost basis is followed there has to be an increase in the rate of return applied to such a base in order to establish an economic rate of return on the property actually devoted to the public use. Indeed, unless the decline in purchasing power of the dollar is recognized in this way the result would be most unfair, and would fail to provide a level of earning power needed to attract new capital unless part of the present equity of the existing shareholders is to be transferred to those who buy new shares.

Q. Perhaps you would like to say a little bit more about that in summary?

A. All this simply amounts to ^{saying} / that we have to start out with some dependable rate base but that economic conditions or considerations indicate in the end that an adequate rate of return, one which will permit the enterprise to obtain additional capital, must be related to the true present value of the investment. As far as I know the only reason for clinging to historic cost as a rate base is that it provides a practicable and dependable figure from which to start. In the end I am bound to say that no rate of return is economically adequate which does not cause capital issues, representing actual investment, to sell at prices such that their total value on an open market will be approximately ^{equal} / the present value of actual total investment, that is, reproduction cost of equivalently useful property less observed depreciation.

Q. Now, having generalized on the subject would you apply your views more specifically to the case of the Canadian Pacific, and in that connection what you suggest as to how a rate of return might perhaps be established?

A. Much of the actual investment in Canadian Pacific

Railway property is represented by fixed interest obligations at 4%. The owners of these issues have of their own volition chosen security and low return as an alternative to the chance of obtaining a higher return. The issuance of senior securities by Canadian Pacific represents a series of contracts between ordinary shareholders of the Company and the holders of specially protected obligations. The burden of executing these contracts falls on the ordinary shareholders. They have assumed that risk of loss, and if there is a profit as the result of that contract it ought to be theirs also. The owners of the company's ordinary stock must obtain a return on the total replacement cost of the property less observed depreciation out of which they can meet their contractual obligations for interest to the owners of the specially protected securities. The test of the adequacy of the return will, of course, be reflected in the market price of the ordinary shares.

Q. Then does that mean that you are suggesting that the Canadian Pacific should have a higher return than it seems to indicate in its submission?

A. Yes, sir, that is true. I believe that the Company's submission is altogether too moderate in its tone on this question of rate of return. As an economist I feel I should warn the company as well as the Commission that the Canadian Pacific should have a rate of return for its shareholders based on the present cost of replacement ^{an} of equivalently useful property less observed depreciation. Dr. H. B. Dorau, in the 20% case, recommended that rates should be established in order to provide a return of at least 8.2% on the net railway investment of the Company of approximately \$1,001,000,000. Mr. Northey Jones in the same case who approached the matter from the standpoint

of a hypothetical capital structure, suggested a minimum rate of return of 7.17% on his estimated capital structure of \$930,000,000. This was equivalent to 6-2/3% on the net railway investment of \$1,001,000,000. It is, however, to be observed that Mr. Jones relied on Other Income to provide what he called a "cushion above the railway earnings of 10%" (meaning an earning of 10% on the ordinary stock) "to give you a premium over the par price which is necessary to sell the ordinary shares at par."

Q. What would you say if conditions should make it impossible for the railway to earn such a rate of return?

A. I do not think that any regulatory tribunal sets itself up as guaranteeing a rate of return to investors in a public utility. Only economic conditions and operating efficiency can determine what actual return will be obtained. What I suggest is that a rate of return calculated as I have indicated should be regarded as permissible, and that the Company should be free to establish rates under this rate of return as a ceiling.

I should like to draw particular attention to a recent publication, National Transportation Policy, by Dearing and Owen, published by The Brookings Institution, pages 293 and following. The argument there leads to the conclusion that it should not be part of the duty of regulatory tribunals to fix maximum rates beyond controlling a maximum rate of return.

Q. What is your own view about that?

A. I think that embodies the correct approach. Implicit in it is a frank recognition that the railways no longer have a monopoly of land transportation. Therefore there is no longer any problem of a potentially excessive general level of rates. The real problem is how to protect the integrity of a necessary capital investment in railway

property. I am not certain that there ever was need for control over maximum rates; if there was it certainly ended by 1920. Practical business conditions will impose a ceiling on rates, without any need of action by regulatory authorities.

Q. Now, what is your view as to the Company's attitude as to the rate of return and the matter of regulation of maximum rates?

A. I believe its attitude is altogether too modest. I firmly believe that, for the economic interest of the nation and of the railways, the railways should be permitted complete freedom in establishing maximum rates up to the point of earning a proper rate of return and that regulation, originally intended only to prevent discrimination, should be limited to preventing unjust discrimination and, by controlling the maximum rate of return, to prohibiting any monopolistic exploitation.

Q. By that you mean you would substitute for the so-called standard rates the maximum provided by the earning power which the Company should be allowed to achieve?

A. Yes, that is up to the point where there was abuse of monopoly power leading to a rate of return upon the capital higher than could be earned in a competitive industry they should be free to establish their rates.

COMMISSIONER ANGUS: Q. Does that mean that there would not be any abuse of monopoly power if high rates were exacted from the part of the traffic that was really a monopoly so long as the total returns to the railways were not excessive?

A. I would think so.

MR. EVANS: Q. What have you to say as to whether that statement would in some way be dependent upon this value of service principle again?

A. Well, I would think of the value of service principle

as being a limit upon it. That is, if the attempt to set rates which would give you the desired rate of return was drying up your traffic then of course that is another question. In the railway's own interest it will back off from such maximum rates.

COMMISSIONER ANGUS: Q. That is true of any monopoly, isn't it, that it aims at the point of maximum return and not at the point of maximum unit price?

A. Yes.

Q. So that no monopolist has any inducement to raise prices beyond the point of maximum return. You haven't got control to prevent that?

A. But surely where you have a regulated monopoly it is at least conceivable that you stop them below the point -- ideally you cut off their earning power at the point at which the earnings on capital just equal the earnings available on competitive capital elsewhere in the economy.

Q. That is treating earnings of the whole system, isn't it?

A. Yes.

Q. There is no limit, other than the interest of the monopolist, to the point up to which a monopoly price may rise if it applies to a very small part of the traffic?

(Page 17854 follows)

A. That is true. I can see no escape from the ^{unless} position/you want to establish regional investment and regional earnings.

Q. Won't there be this escape from the position, that the people who have to pay those supposedly quite high rates will argue that they have a case, not against the railways but against the Government, to provide them with a road so that they will have competition?

A. Well, I think I am widening the discussion, but as I see the present situation you have railways which are under regulation, you have specially a private railway subject to corporate income tax, and you have other forms of transportation under the most enthusiastic promotion by Government. Now, surely if you backed off from the promotional activities in relation to the air, in relation to motor carriage, in relation to water carriage, you might again come fairly soon to the position where, with no further increase in the higher rates, and with no rate at all unreasonable, you still had a reasonable rate of earning power on the capital investment in railways.

Q. I am thinking of this case quite simply; you have, as you say, promotional activities that give you competitive services by air, by water, by road---

A. At less than their cost.

Q. A, B, C and D; now E comes along and says, "Where I am situated there is no canal, there is no road, I get no benefit from competitive services, therefore I have a claim either against the Government for putting in some competitive services or I have a claim for subsidization or compensation because the Government has favoured others and has not favoured me." I mean, you can see how that would work up to a political claim, whatever its merits?

A. Yes. As a political claim it seems to me that if you help E you must prepare tomorrow to help F, G and H, and the day after you run through the alphabet.

Q. That would apply to the monopoly^{sector} of the railway traffic if the rates of that sector became very much higher than the other rates?

A. Yes.

COMMISSIONER INNIS: Q. What tests would you use as to maximum traffic from the standpoint of earnings?

A. You mean a test as to maximum earnings?

Q. Yes.

A. Well, I would think that the market test is the only objective test I know.

Q. That is, the earnings themselves?

A. Yes. That is, with a growing railroad, if you have the market price up to your book value, then at that point you are ready to cut in, as regulation has a point to make.

Q. I think we are perhaps arguing about different terms. Let us take this test -- the number of empty cars moved; would that be an ^{indication} to you as to whether you are charging too high rates or too low?

A. I do not think so, because empty car movement is determined by the kind of traffic you are getting and not by the amount of earnings you are making. If you have coal traffic you are going to have as much empty as you have loaded. Box car traffic, you will probably get let us say 70 per cent load to 30 per cent empty.

Q. Yes, but suppose you had some fluctuations over a period; your empty car movement was declining, or your empty car movement was increasing; would^{you} regard that as an indication as to whether rates were too high or too low?

A. I do not think so, sir, no. I cannot see that that

really bears closely on the problem.

Q. The use of the railway's equipment, is it not a factor?

A. Well, you are talking about empty car mileage or of idle car days?

Q. Both.

A. Well, as to empty car mileage, I think that is something pretty nearly required by the nature of the traffic handled. I do not think it bears directly on earnings at all, that is, on whether earnings are adequate or inadequate or overly adequate. Now, if you have let us say a huge car stock unused through the peak season of traffic, it can mean any one of several things. It might mean a general business depression. If it happened in a year of prosperity it might mean an over-investment, and in that case your Commission might say, "This railway is not investing wisely; it has provided more cars than are called for."

Q. But it would never mean that rates were too high?

A. I cannot see how it would, except as I say, you establish a proof that the railway did make such an egregiously bad forecast of its traffic that even in a period of high prosperity it had more cars than it knew what to do with.

THE CHAIRMAN: Q. Would that be because the traffic would go elsewhere, or not budge at all? Which have you in mind?

A. Well, you are really envisaging a departure of traffic from the rail so fast that they are left high and dry?

Q. Well, take an era of prosperity?

A. Yes.

Q. Still the cars are not moving?

A. Yes.

Q. Well, is it because people have just simply stopped shipping and receiving?

A. No.

Q. Or do they give their traffic to trucks and to other modes of conveyance? What happens?

A. I had thought of it in the first place as being a matter of buying too much equipment, that they just did not gauge their requirements properly.

Q. They are overstocked even for a period of prosperity?

A. Yes. Now, in that case you might say that the rate base is too high, by including these excessive cars.

MR EVANS: I was wondering whether Dr. Innis did not perhaps have in his mind something like this, that if you found, having a given traffic level and an increase in rates, a sudden drop in traffic which rendered those cars idle, would that indicate that your rates might have been pushed too high?

COMMISSIONER INNIS: That is right, that is the sort of thing.

THE WITNESS: That is idle car days, isn't it, rather than empty car mileage?

MR EVANS: Q. Yes, but I think Dr. Innis was envisaging, if I got him correctly, a condition where management had acquired what it considered to be necessary for the volume which it foresaw, and then, due to higher costs, it got an increase in rates, and that was followed immediately by a drop in traffic rather than a certain number of cars idle, and I think Dr. Innis wanted to know whether you would consider that as an indication that rates might have gone too high?

A. Well, that is an indication which the traffic

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department of the railway would very properly take into account.

THE CHAIRMAN: In doing what? In fixing rates?

A. In perhaps reducing rates from where they were first set. But the railway ought to be allowed to do that or fail to do it. It should not be compelled to do it by the regulatory board, because if the regulatory board steps in when earnings are still below normal earnings, then I believe that they are ^{substituting} their judgment for the judgment of the railway officers, and they are not equally taking responsibility for the results of that exercise of judgment.

COMMISSIONER ANGUS: Q. Do I gather that the regulatory board would not step in except in two situations -- one, if the net earnings of the whole system were above what was permissible, and, two, if an individual rate were discriminatory?

A. Yes.

Q. And it is under those conditions that you want the Crows Nest rates put at the disposal of the Board?

A. Yes.

MR EVANS: There was one other question I made a note of; I do not know whether I am too far removed from it, Dr. Angus. You put a question a minute ago, and I made a note to come back to it. I do not know whether you had it cleared up to your satisfaction. You were talking about this maximum return, and I had in mind putting a question to Mr. McDougall based on it, but I was wondering whether you were distinguishing in your question between the maximum return in the economic sense and in the regulatory sense.

COMMISSIONER ANGUS: Between what?

MR EVANS: The maximum return in the sense that

you got all you could out of traffic before it began to diminish, and in the regulatory sense where you had a permissible maximum which might not coincide with the maximum return in the economic sense.

COMMISSIONER ANGUS: No. What I suggested was, I understood that the maximum return in the economic sense was being spoken of as an effective ceiling, and it was suggested that that would operate even if the regulatory control were not invoked, because the total earnings had not come up to what was allowed.

MR EVANS: I thought perhaps you had been talking in the economic sense, and I thought perhaps you might have been at cross purposes with Mr. McDougall, because I feel sure that what he has been discussing here is the maximum return in the regulatory sense, that the return permitted by the regulatory authority would provide the maximum limit over all for rates. Perhaps I misunderstood both of you.

COMMISSIONER ANGUS: Q. Have we been at cross purposes?

A. I thought that the maximum regulatory return would probably be arrived at before you had come to the point of the maximum economic return.

Q. I rather understood that we were suggesting that if competition prevailed in parts of the system and monopoly in other parts of the system, the monopoly rates might go very high before the regulatory control could be invoked, because it depends on the earnings of the whole system?

A. Yes.

Q. Right so far?

A. Yes.

Q. Then I understood that you were replying that the

monopoly sector would benefit by what is called the economic ceiling, that the railway in its own interest would not put the rates higher than the point of maximum revenue?

A. Yes.

COMMISSIONER ANGUS: I do not think there is any misunderstanding there.

MR EVANS: I am sorry; I thought perhaps there had been.

COMMISSIONER INNIS: Q. You would not be inclined to go so far as to do away with regulation altogether?

A. Oh, no, by no means.

Q. What is it you want regulation for?

A. Discrimination. After all, your Interstate Commerce Act was set up for that particular purpose. We followed it here in this country. The idea of regulating the maximum return comes in at 1920. It is introduced for the purpose of protecting the railways. It was this new charter for transportation, and it has become inverted in fact.

THE CHAIRMAN: Q. Does your definition of what ought to go on absorb the present requirement of the Act that all rates should be just and reasonable?

A. Yes.

Q. And fixed---

A. Because I think that comes under the general idea of discrimination.

Q. Fixed and maintained by the Board, the Act says?

A. Yes.

Q. And at a just and reasonable level; you are providing for all that, you would think?

A. I would think so.

Q. That is, just and reasonable towards the shipper as well as towards the railway?

A. Yes.

Q. You arrive at that result by the machinery that you set up?

A. I think so.

COMMISSIONER INNIS: Q. I find it pretty difficult to understand a situation in which you would allow a great deal of traffic to remain idle, and the public would not be concerned in the fact that that equipment is not being used.

A. I was setting up a wholly hypothetical example, I thought. Obviously, nobody wants idle equipment, the railways least of all, and I was saying that in this hypothetical example if you had an excessive overbuilding, then the Commission might say, "This was an improvident investment of your capital, and you will be compelled to bear the burden of it."

THE CHAIRMAN: Q. With what consequences?

A. That the rate base would be proportionately reduced, and the allowable earnings similarly.

Q. And then the rates would go down?

A. Yes; that they would not be allowed to expect a return upon a redundant investment.

Q. Well, that would operate as a lesson for the future, I suppose?

A. It would operate as a penalty in the present and a lesson for the future.

COMMISSIONER INNIS: A hypothetical situation which is very, very hypothetical.

THE WITNESS: Oh, yes; there is no shadow of that. On the contrary, I would think that the railways would give better service and make more earnings if they had additional

investment in them. I think that was the whole burden of Mr. Newman's evidence.

MR EVANS: One point that perhaps might be interesting in that connection, Dr. Innis, is the statement made by Mr. Newman, that the aim was not to provide equipment for the maximum volume of traffic, but to provide it for the average volume, so that in periods of maximum volume you could always get a very fine degree of utilization, which enabled you to make the best use of it.

Q. Now I might turn to another subject, Mr. McDougall. I gather that you have read that portion of Part II of our submission dealing with the Manitoba proposal that railways should be regarded as instruments of national policy?

THE CHAIRMAN: Pardon me a moment. I think perhaps I might ask a question now of you. You have been asking Professor McDougall right along whether he does not think that your submission on the matters about which he has been talking was rather too modest or too moderate. Do I understand that you are changing it in any way?

MR EVANS: No, sir.

THE CHAIRMAN: Leaving it as it is?

COMMISSIONER INNIS: You mean you were not able to persuade Professor McDougall---

MR EVANS: He has expressed his views, and he won't be held back on that. I let him express them. They certainly did not originate with me.

THE CHAIRMAN: All right, go on, Mr. Evans.

MR EVANS: Q. I was about to suggest to you that you had read the discussion in Part II of the Canadian Pacific brief, and to ask you your views upon the proposal of Manitoba, that railways should be treated as instruments of national policy. Would you comment on that?

A. Well, it seems to me, sir, that a good deal of what

is said by Manitoba on this topic stems from an imperfect appreciation of the historic conditions out of which railway subsidies---

THE CHAIRMAN: Q. Stems from what?

A. An imperfect appreciation of the historic conditions out of which railway subsidies arose and that the recommendations for the future are badly designed to achieve the situation which the province regards as desirable.

MR EVANS: Q. Would you elaborate on that a little, Mr. McDougall?

A. Well, subsidies were given in this country for the building of railways for two very good reasons. The first was that the necessary capital investment was very high in relation to the capital available in the country, and it was especially high in relation to the probable initial gross earnings of a newly built line. Therefore it was very difficult to finance railways at all; and even if the ultimate success of a railroad was clear, it was hard to tide the new railroad over the early years until those major structural changes had taken place in the community served which brought the two into a living unity and identity of interest.

Q. You spoke of two reasons; was there another?

A. Yes. The second was the extraordinary efficiency of rail against road carriage. Even a poor and cheaply built railroad could make money carrying a ton at the rate a carter by the road would charge for hauling a hundred-weight. This provided the incentive to the community to use its credit to raise money to be paid to the railway as a subsidy. The community could well afford to do so with profit to itself. Those settlers who were already established would profit greatly by having the railway available; and territories which could either not be settled at

all or which would be settled slowly with great privation by people who went in advance of railways, could be settled easily with railways. My own reading of the motives of those who made policy at the time is that they thought of subsidies as a means of speeding up the development of a privately owned railway network and nothing more. They were encouraging the early stages of a development which would thereafter be self-sufficient and self-supporting.

Q. Well, would you say that that exhausts the subject?

A. No, sir, but I think it does cover it pretty completely down to, say, 1900, when the first construction period ends. In the present century estimates of growth were made with an exuberance which led to excesses, and those excesses had later to be corrected.

Q. Then do I gather that you do not think that the policy as shown in the early days when these subsidies were granted necessarily meant that the policy involved treating the railways as mere instruments of national policy?

A. No, sir, I do not think so; certainly not in the terms that Manitoba uses. They thought of the private railways as an integral part of the national economy. They knew that a country properly supplied with railways was far more productive than one which lacked them. But railways were to make their contribution to the national well-being as independent units in a symbiotic relationship with the rest of the country.

Q. Why do you say that?

A. Well, if that were not so, then the Railway Act would be to me an unintelligible piece of legislation. If railways are and ought to be wholly subordinate to the Cabinet of the day; if imponderable considerations of public

policy are periodically going to require interference with their operations; if their claim to financial independence is always to be regarded as secondary to those considerations of public policy, then what was the point in setting up a quasi-judicial body -- the Board of Railway Commissioners -- to adjudicate between the railways and the public, respecting the rights of each and requiring each to fulfil its correlative duties? For myself, I can see no point whatever in this administrative machinery except upon the assumption that the railways are expected to be independent.

Q. Now, have you anything to add on that same subject?

A. Yes, I think there is one more significant point, and that is that when the majority of the Drayton Commission of 1916-17 recommended the setting up of the Dominion Railway Company to own and operate the railways which later became the Canadian National Railways, it made the complete independence of that company from all political and governmental interference---

THE CHAIRMAN: What year did you say?

A. 1916-17. It made the complete independence of that company from all political and governmental interference the foundation stone of its proposals.

Q. Do you mean to say that was in the statute, for instance?

A. Oh, no, sir. This is the recommendation of a Royal Commission.

MR EVANS: The Drayton Commission, my lord.

THE WITNESS: It was not only to be independent, but the trustees who were to operate it were to be a wholly self perpetuating body. The Government would receive the dividends which that company was expected to pay after a few years and could use that income to reduce taxation, but it was to have no voice in the management of the company

even on the most important of long-run questions.

MR EVANS: Q. Now, what is your view as to whether it is desirable that railways, or at least some of them, should be privately owned?

A. I think they should, sir. The primary reason is that I am conscious of the dangers that follow from the concentration of power. I do not believe it is possible to expect that railways could remain self-supporting if they were to be regarded and dealt with by the government of the day as mere instruments of national policy.

If all railways come under public ownership because that was the only way in which they could get funds, they would inevitably come under the thumb of the government of the day, which would have to recommend to Parliament that it vote those funds.

I say that is the major reason, that Government, which already has a very large finger in the livelihood of the average man, would have a whole hand in if it took over the railways too.

Q. Have you other reasons? You say that is the major reason.

A. Yes, sir, I say so for more narrowly economic reasons also. So long as we remain a democracy---

THE CHAIRMAN: Q. Are you not reciting what would be inherent? If the Government took over all the railways, of course they would all be Government railways, like in England today or in France today.

A. And it is the impact---

Q. For the last seventy-five years in Germany; you had Government ownership of all the railways in all those countries.

A. But is it not the impact of Government control---

Q. Are you not describing merely the necessary conse-

quences of Government ownership?

A. I think so, yes -- just so we are both agreed that it is the impact of that strategic power reaching into every corner of the economy. Making railways wholly public properties would mean a vast extension in the power of government over what it now is in this country.

Q. In this country?

A. In this country, yes.

MR EVANS: Q. You were going on to give other reasons?

A. I say there are narrowly economic reasons also for holding to that position. So long as we remain a democracy---

THE CHAIRMAN: Q. What you have said so far does not seem to me much more than saying that Government ownership means Government ownership. We know that. That is, you say if the Government takes over all the railways it has all the railways; of course it has.

A. It not only has all the railways, it has a control over everything that moves through the railways, which may be a very much bigger thing, especially if there is anything like the chance to distribute either rate favours or wage favours.

Q. Well, have you studied those incidents in relation to what did take place in other countries when Government ownership became effective and was carried on?

A. I have read some, yes.

Q. It is going on in England today?

A. Yes.

Q. But of course that is---

A. It is too soon to get much out of it, but in relation to Germany, you were not bothered with the particular difficulties of democracy.

Q. Why?

A. Well, because in the imperial regime, pre-1914, you did not have the Kaiser depending to the degree which our Government does upon the vote of the Reichstag.

Q. Well, there may have been a degree of difficulty, but you had the Reichstag, and you had elections, and you had deputies, what we call members.

COMMISSIONER INNIS: And Parliament responsible to Cabinet.

THE CHAIRMAN: And in France, too, you have even more so; you have a little too much of it there.

COMMISSIONER ANGUS: Were the railways imperial railways or Prussian and Bavarian and so on?

THE CHAIRMAN: I think they were imperial.

THE WITNESS: I believe you are right, that they were Prussian; they became imperial, at least they became the Reichsbahn, in 1923 or 1924.

THE CHAIRMAN: Q. Before that they were state railways?

A. You see, up until 1914 they were not only self-supporting in Prussia, they were the source of considerable profit, and it was therefore possible for a strong bureaucracy to hold them out from the control of the legislative body in a fashion that we have not yet found in this country.

THE CHAIRMAN: Q. Well, you are telling us, then, the dangers you would see from complete Government ownership in this country?

A. Yes.

Q. Can you lead to that by what you have seen of partial Government ownership in this country so far? -- because it is a pertinent question, you see. I do not want to embarrass you.

(Page 17871 follows)

A. Well, the final passing of the accounts of the Canadian National Railways is done by a Committee of the House of Commons.

There is a passage in the 1926 Report of that Committee which is, to me, immensely significant.

Mr. R. A. C. Henry was then chief of Research and Development, and he produced a very competent study of the variations in expenses of the railway in the year 1925.

Knowing something of the technique involved, I realize how much work went into that study and how carefully it was designed to be a full report, and yet one which was clear and intelligible.

The report was made, and the next question was: "Who did you buy ties from in my constituency?"

It might as well not have been made, because members of parliament are busy, and to them a House Committee is only a small part of their duty and responsibility. They just do not have the time to sit down and to sweat through what was in fact a multiple correlation study.

Q. I was wondering just what the answer to that question was?

A. I am sorry. I can carry some things, but not too many.

COMMISSIONER INNIS: Q. Labour used to be more powerful under a system in which the railways were owned by the government?

A. I would think so. If you have a bloc of people with interests spread across the country, then those who are bidding for their votes will consider them. It is inevitable.

Q. Why would labour be opposed to amalgamation?

A. I would think it is like many other things, that while amalgamation might, in the end, produce a greater number of votes, nevertheless the powers feel that in the short run -- and it is the short run they are probably considering -- it might mean a reduction in the staff employed and therefore they are against it for that reason.

They can answer it better than I can. But that is my reading of it.

Q. You mean that labour is just short sighted?

A. Aren't we all mostly? I thought that was my major contention in relation to rates this morning.

MR. EVANS: Q. Now then, you have come to what you said was a major reason for your views that there should not be public ownership of all the railways in Canada; and you said there were also other reasons, which you called narrow economic reasons. Would you say what you think they are?

A. So long as we remain a democratic people, interests will be able to put pressure upon the government, and especially when elections impend.

If all railways are government owned then there will be short-sighted pressure to preserve the outmoded, or to compel the introduction of additions which are uneconomic. Moreover, we would be open to log-rolling between geographic areas to extort local benefits.

At the present time the existence of private competition as related to publicly owned property puts a certain natural limit to that kind of pressure which can be applied when there is full public ownership.

Furthermore, I believe the present situation

is better, even from the standpoint of those who complain about it at the present time. There is competition between the two railways.

I know, from talking to small shippers, that this gives them a leverage which no regulatory body could give.

The withdrawal of even small traffic from one line will bring an earnest ^{study} of the grievance complained of and a correction, if that is possible.

However, if there were a railway monopoly, there would be less interest on the part of management in correcting such situations; and moreover it would be compelled to work against a body of employees who ^{be} would/only too conscious of the monopoly power of the railways and whose unions, under the new situation, would go far to fulfil theoretical gains.

Anyone who knew the situation in Canada before competition became effective would testify that the unionization of some employees has a tendency on others to use their position for private gain. So there would be much more discontent than there would be complaints about rates or anything else directed to the management.

Q. You think that competition is a very important factor to be borne in mind in dealing with this subject?

A. Yes. I think competition is both flexible and productive.

In the late war, the wartime Prices and Trade Board attempted to control prices. It was recognized that regulation was not half so effective as the spur of direct competition. I believe this must be so.

No matter who regulates, or how much effort

is put into it.

Regulation can, at best insure that operations are carried on with a certain modest incompetence; but active competition with efficiency as the price of survival will produce results.

Q. Have you anything further to add on this subject?

COMMISSIONER INNIS: Q. Do I infer that the competition was anything more than competition in service?

A. There is definitely competition in service, yes, and that is protection for the small shipper.

Q. You are not suggesting that there is any competition in rates?

A. No. Although I will suggest that when they sit down in the Canadian Freight Association, there will have to be a matching of views, in which one line may well be the spokesman for the shipper.

MR. EVANS: Q. When you say "spokesman for the shipper", had you in mind the case of a line which had quoted a rate to a shipper trying to get that rate on behalf of competitors?

A. Yes.

Q. Is there anything else you would like to add on this subject?

A. I have said that leading the railways in private hands with reasonable earning power and real independence of action tends to diffuse power and fosters a continuous interest in giving good service.

I envisage vigour and vitality in the private operation. If it is devitalized by the denial of earning power and by an excessive regulation, then there

is no particular reason to expect much from it.

The management must have responsibility and authority. If it hasn't enough free money to permit it to keep up in the railroading art by improvements to its line and by the purchase of new equipment, if it dare not show initiative but must wait for permission or even for direction from the regulatory body, then the fact that the property is nominally in private ownership is of relatively minor importance.

COMMISSIONER ANGUS: Q. The more strictly regulated a private interest is the more advantages there would be?

A. I would think so, yes.

MR. EVANS: Q. At the bottom of page 6 of Part II of the brief there is a sentence which reads as follows:

"Canadian Pacific believes that private enterprise in the railway field does require regulation, but that the need for regulation becomes less and less as the railways lose their position of semi-monopoly in the presence of increasing competition of other forms of transport."

Would you care to express your views on that submission?

A. I am in full agreement with it, with that statement.

Comprehensive regulation was one thing when railways had a monopoly of land transport; it loses much of its justification when railways are exposed to competition on all their high-grade traffic.

Even under monopoly the formal defence of regulation was that it was meant to prevent exploitation of monopoly power. The same principle is valid when the shoe is on the other foot.

It is a perversion of justice to use the regulatory mechanism to prevent the railways making normal earnings upon their real investment. If they are no longer a monopoly they should no longer be treated as one.

Q. What do you view as changes which have taken place, and which will take place, if motor competition is to continue?

A. I find it very hard to visualize what must come there, because motor carriers are probably going to increase in importance. But the response to that situation is, I think, as obvious as it is inevitable: that the railways must be allowed to increase rates on their low-rated commodities to offset the loss of revenue on the high-rated commodities.

I question whether there is any real hope of a correction in the situation presently ruling until the railways are able, by raising rates on the low-rated commodities, to make the public realize the full cost to them of the present unfair competition.

COMMISSIONER INNIS: Q. You do not think that regulation will become more and more necessary as competition became more intense, to consider it in a reverse position?

A. No, I do not think so, and for one very good reason: that if motor competition is entirely a provincial matter, I do not see how you are going to rectify what was done, or what is being done,

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by the provinces, by narrowing the railways in by still further regulations.

Let me suggest this: that when the railways had a monopoly power, when they were the major carriers, then you established a certain rate structure which was appropriate to that condition.

Now, if I understand a good deal of what has gone on the record of this Commission, it is an attempt to retain all the fruits, while refusing to recognize the changes in the fundamental bases which produced those fruits; and it seems to me there is a conflict there which is too great to be allowed to go unresolved.

Q. What about others in the intense competition in the transport business being more serious than a monopoly?

MR. EVANS: You are thinking of rebates?

COMMISSIONER INNIS: Yes.

MR. EVANS: We are not asking for that to be removed.

THE WITNESS: That comes under the general head of discrimination and it is such a vicious kind of discrimination it would certainly be the last thing to come.

THE CHAIRMAN: We shall now take a short recess.

Recess

Upon resuming:

MR. EVANS: Q. Prior to the adjournment, I had put to you, and there had emerged from it a considerable amount of discussion, about a suggestion of

Manitoba, that the railways should be regarded as instruments of national policy.

THE CHAIRMAN: Instruments of what??

MR. EVANS: Instruments of national policy.

Q. Now then, Manitoba also raised, in its brief, a suggestion that the railways were really the delivery department of the Canadian economy which was being run by the government of Canada.

Would you make any comments you may feel desirable on that concept?

A. Well, I can only interpret this as a concept which would be consistent with complete government ownership of railways.

The suggestion that the railways are the delivery department of the economy reflects an idea that this country is a single and totalitarian business institution operated by one Board of Directors.

On the contrary, Canada is as yet a free economy in which various economic interests cooperate with each other on terms which are arranged by a process of bargaining.

Unless we are prepared to abandon that in favour of the totalitarian theory, one cannot approach the matter of regulation of railways on the assumption that they are merely the delivery department of the economy.

COMMISSIONER INNIS: Q. What is that word? Is it "delivery"?

MR. EVANS: Yes. You will find it discussed at some length at pages 13 and 14 of Part II of our brief; and it comes from page 3 of Chapter III of the Manitoba brief.

THE CHAIRMAN: Q. After all, we must find some word? What part of the economy are they? The carriers operate. What objection to the word "delivery" is there? They are part of the economy.

A. That is right, they are part of the economy.

Q. Then how would you describe them if you do not like the word "delivery"?

A. I think the implication in the term used was that they were merely a subordinate part without any independence, and that they took orders but had no real right to determine what would happen.

Q. "Took orders" from whom?

A. From whoever was head of the firm.

Q. Head of what?

A. Head of the firm. In this case, whoever controlled the Canadian economy.

Q. You mean the Board of Transport Commissioners?

A. I mean our Cabinet.

Q. The Cabinet of Canada?

A. Yes. I think the distinction would be this: A delivery department for a store is one department of that store under the general manager.

But if the store enters into a contract with a private carrier to deliver its parcels at so much each, or so much per hundred pounds or a combination of the two, then that carrier is a private carrier. And I think that is a much clearer and closer parallel to the position of the railways to the Canadian economy than is the idea of a delivery department under the thumb of the general manager of a store.

Q. I would suppose that the Manitoba brief in using this word would go on to tell us what they mean?

MR. EVANS: It is page 59, Chapter III of the printed brief entitled "Manitoba's submission". The Chapter is entitled "Railway Service - Standards and Cost".

The opening paragraph reads as follows:

"In the preceding two chapters we have dealt with the philosophy and attitude which, in our view, should underlie the changes which your Commission will recommend in the legislation and the administration which controls railway operations in Canada. We now turn from these discussions of general matters to a more specific consideration of certain aspects of the policy which, in our view, should be followed in the future."

This is their concept of regulations brought into very specific terms; and then they list three things:

- "(a) the standard of railway service which should be made available to Canadians;
- (b) the methods of determining the total expenses necessary to provide that standard of service;
- (c) The methods by which the amount of revenue necessary to cover those expenses is to be secured."

And then they start out to discuss the standard of transportation service; and at the bottom of page 60 this is the concept of the delivery department:

"The relationship between the people of Canada and the railway system is, in this regard, somewhat similar to the relationship between a large retail merchandise establishment and its delivery system. The problem is to decide the type of delivery service which is to be provided, which includes such questions as the frequency of deliveries to the customers, whether those deliveries are to be made in new modern trucks, or in older, cheaper vehicles, and what proportion of the total revenue of the establishment is to be set aside to pay for the delivery service. One method of dealing with these problems would be to allow the manager of the delivery department full authority to settle them himself. So long as the total area served by the establishment continued to expand rapidly, and the number of customers and the volume of goods to be delivered continued to expand with it, it might be quite satisfactory to leave these matters in the hands of the transportation manager, for his natural tendency to expand and improve delivery service would be quite in line with the needs of the company. But it would always be clearly understood that his decisions were subject to review by the general manager of the entire organization. Once the full area which was tributary to the store had been supplied with regular delivery service, there would eventually come a time

when the general manager would need to assert his authority over the transportation manager and see that the activities of the delivery department were not inconsistent with the needs of the whole company in the new circumstances. It is our view that Canada's railways have now reached that position."

It is with regard to that that Professor^{McDougall}/has been directing his evidence.

MR. EVANS: Q. Now then, had you completed your answer on that question as to your opinions on it?

A. Yes sir, I had.

Q. Now then, at page 57 of Part II, we are now in the brief dealing with the matter of horizontal or flat percentage increases in freight rates, and the following appears:

"In following the argument, it should be remembered that the rise in the general price level has been the moving factor in compelling rate increases, certainly since 1946 and practically since 1914."

Would you like to comment on that paragraph?

A. That seems to be nothing more than a recital of obvious facts.

Railways are an integral part of the whole economy. They ^{are} y coal, steel, lumber and all their other supplies in competition with the rest of the community. They must compete with other employers for the services of labour.

There is no conceivable way in which they can be insulated against general changes in the value of money. Therefore when prices rise sharply, they must

be allowed to share in the general movement. But just because their selling prices are regulated there has always been resistance to this perfectly normal re-adjustment, much of it by people who had themselves already raised their own selling prices.

Q. Yes.

A. The railways were prosperous under the rates and costs of 1914. It was the external force of a general inflation that caused the rate increases up to 1920.

The railways were distinctly not prosperous at 1939 because the Canadian community was so depressed at that time that the volume of traffic was unduly low, but they did not ask for increased rates to compensate them for the fact as the American railways did in the 1930's.

Upon the contrary they reduced many rates. They did not ask for an increase in rates until 1946 when the inflation was already far along. It might have been better for the nation if the railways had raised their voices much earlier than they did.

Q. That has been a condition in all parts of inflation, that we have had this public clamour of this kind.

A. Yes, I think of the nearly inevitable consequences of regulation under inflation, because people become used to particular prices, and they do not make a connection between an increase in the value of income to them and of an increase in the cost to those who provide the service.

And then, towards the end of every great inflation, the public has got to be re-educated to the

idea that general price changes have got to be truly general. And I say with some regret that this process has not yet been completed in Canada.

COMMISSIONER ANGUS: Q. Do you contemplate that there will be a great many increases in freight rates at frequent intervals, that is, a great many small increases, rather than a few big ones, if they are to keep pace with a rise in prices?

A. No, I do not. I would think that the railways need not appear more than twice in a year. It all depends on the rate at which the wages and other prices are changed against them.

Q. You estimate twice in a year?

A. Twice in a year. For a period, in 1946 to 1947, your prices went up, wholesale, by about twenty points in twelve months. I would think that there you would be probably compelled to do it twice.

Q. And you think that changes in the wages of labour on the railways should ^{occur} / twice a year, too?

A. Well, if wages changed twice in a given calendar year, I would think that the rates ought also. But is your question: Should labour be open to re-negotiate its contracts every six months?

Q. Yes. If you are thinking of smooth increases in which the railway rates climb along with other prices, should they not all go together?

A. Yes, I would think so. I am not welcoming it, mind you; but I would say that if you are going to have a general inflation, it ought to be general. And if the railway unions make an agreement for twelve months, then I think they should live up to it.

COMMISSIONER INNIS: Q. You do not say

anything about deflation.

A. It has been a less urgent problem recently.

Q. But a very urgent problem in the depression?

A. Yes, well, in the last depression, while you did not have any formal reduction in rates, you had a fairly continuous whittling away. And secondly, you had such a low volume of traffic, it was, I think, particularly clear to me at least that the railways were getting by only by such a reduction in their expenses and outlays on maintenance as could not have been permanently supported.

Q. I was wondering in this paragraph which you read, Mr. Evans, where you referred to a rise, whether you could substitute the word "decline" in the general price level?

MR. EVANS: To make it read that a decline in the general price level would be a moving factor in compelling rate decreases?

COMMISSIONER INNIS: That is right.

MR. EVANS: Q. What do you think about that?

A. I would say this: that if it had proven possible to achieve a reduction in wages and rates by the railways in step with other general reductions, then I would say that the next thing which might very well move ^{would be} your freight rates -- but I tried to meddle in that at that time and I got nowhere.

THE CHAIRMAN: Q. You say there might be a revision of freight rates every six months?

A. I was talking about the period of acute inflation such as we had in 1946 and 1947, especially the period roughly from March, 1946, to close to the end of 1947.

COMMISSIONER ANGUS: Q. In discussing inflation and deflation, are you assuming that the volume of traffic is constant?

A. Well no, I cannot, because I will take it that in an inflation you will probably have some stimulation which will tend to increase your volume, and that no matter how ultimately desirable deflation will be, its immediate effect will be towards a reduction in the volume of traffic.

Q. Would you look for this when you compute an increase in freight rates in one case and a decrease in the other?

A. Oh yes.

MR. EVANS: Q. Well then, we have been hearing from you your views that the public needed to be re-educated to these conditions after a period of inflation; and I noticed the following paragraph which gave rise to that answer, at page 57 of Part II of the brief, where I read as follows:

"The argument proceeds, therefore, from a 'normal' situation in which rates are in balance with other prices and with the needs of the railways."

(Page 17897 follows)

Does that express, perhaps in another way, what you had in mind in answering the previous question?

A. Yes, sir. The situation is normal when prices are in balance one with another and when trade proceeds freely for that reason. I may add that an inflation has, almost inevitably, a disruptive effect upon such a situation. It may produce a feverish activity for a time, but it is definitely not wholly a healthy activity. Prices get out of relationship with one another and serious dislocations arise.

Q. How does that relate to transportation?

A. Transportation is an integral part of the whole process of production and distribution. It involves costs. Money prices are reflections merely of those real costs. When costs rise generally, railway costs rise with them, and therefore railway rates, which are the selling prices for railway service, must rise also.

Q. Now then, this section of the brief, part 2, in effect argues that increases in flat rates in cents per hundred pounds are undesirable. Would you care to give your views on that subject?

A. Yes, sir, I agree with that position, and I think the examples given at pages 57 and 58 of part 2 of your brief explain why these flat increases are undesirable under such a price situation, and I emphasize that it is an argument directed at the particular price situation which we have experienced over the last four years. Let me argue it out in this way. Looking at page 57 at the bottom of the page, the normal condition there assumes that there are differences in transport costs, and those differences are offset by other advantages on the part of the distant producer so that the mill net prices, that is, the 96 and 92, include equal amounts of profit.

Q. There you are comparing those two columns, produced near the market and produced far from the market?

A. Yes, and the mill net price, 96 near the market and 92 far from the market and transportation in one case double the cost in the other.

Q. Yes?

A. I am assuming this is normal, that these people are going to continue to produce, and that they will make approximately equal amounts of profit per unit of product in these two different situations.

Q. Now then, would you proceed with what you were about to say about that?

A. Now then, if you follow through the examples B, C and D on page 58 you will see that any change in freight rates other than a percentage change is going to distort the relationships between these two producers, and it is going to increase the profits of the more distant producer. Look, for example, at example B. You have doubled your market price and your transport cost is unchanged, and your mill net prices are now 196 and 192, so that the spread between them, which under the normal situation was 4.35% becomes 2.08. In other words, the distant producer is now able to make more profit out of a unit of product, other things being the same. He is able to bid for labour and for the services of the factors of production. He is advantaged by the fact that selling prices have increased and his transport costs have remained unchanged. It is therefore a pressure to build up production at the distant source.

Q. Yes.

A. Now then, example C takes an increase by a flat amount, that is, in place of a transport cost of 4 and 8 you now have 7 and 11, but the difference upon your ratio

between mill net prices is almost negligible. Comparing examples A and B it was 4.35 to 2.08. Comparing A and C it is 4.35 to 2.12; in other words, it is not significant.

Q. What you say then is that under C the position is relatively the same as though you were under B?

A. Yes, it is almost the same as if you had made no change whatever.

Q. Yes?

A. Now, example D has a 50% increase in transport charges, that is, you are approaching the kind of change that took place in prices.

Q. Yes?

A. But you have still moved only half the way back to your normal situation.

Q. Normal being to get back to the original position; market prices having doubled your rates are double to get back to exactly the same position as you were in when you had item A?

A. Yes. Under D you have the same situation in which some bonus, some additional encouragement, is given to the distant producer.

Q. And that is demonstrated by what?

A. Finally when you come down to E where you allow both prices and transport costs to double you have restored your normal situation.

Q. Then you get exactly the same result as you had under item A?

A. Yes.

Q. Now then, have you any further comment to make on that?

A. Well, I am not saying that the more distant producer would not like to retain this spread in his favour. We are most of us ready to take all we can get and then to look

hopefully round for more. What I am saying is that railway rates are prices charged for services given. Giving services involves costs which must be met in some fashion. If the money cost of giving service increases then so must the price at which it is sold.

Q. Then what do you say about attempts to deal with a situation of that kind other than by percentage increases?

A. I think, sir, it is going to result in distortion in the distribution of population and industry, that so long as it remains the distant producers will be given a special advantage in bidding for resources, that the amount of transportation used fruitlessly will be increased, and in the end the community will be worse off until economic pressure restores the old normal percentage relationships. That is, of course, assuming that there is no fundamental change in the techniques of transportation. If you could wave a wand and cut costs by half you have a new situation. I am merely saying that until something of that kind happens so long as the old situation remains then you ought to try to go back after your inflation to those relationships which held before it started.

Q. Now then, I would like to take you to a different subject. The Commission will find this subject dealt with at pages 128 to 134 inclusive of part 2 of the Company's brief. Mr. McDougall, have you read the submission of Alberta on the subject of Industrial Location and the Rate Structure?

A. Yes, sir.

Q. Would you give the Commission your views on the argument made in that brief of Alberta?

A. Well, I believe, sir, that this is a particular example of that general failure to recognize the life process of an economic society of which I have already spoken. It is quite clear to me that Alberta will develop an increasingly diversified manufacturing industry based on the raw materials which are now ^{known} and whose exploitation is now proceeding at an increasingly rapid rate.

THE CHAIRMAN: Q. Tell me, what raw materials have you exactly in mind?

A. I am thinking of oil and gas above all else.

Q. Just those two?

A. Well, those two particularly, because of so much that can follow from them.

Q. Are you thinking of meat, for instance, cattle?

A. Yes, but I would think that oil and gas, being both power and potential chemicals, you are going to move into a very important development in that province inside the next ten to fifteen years. The very fact that you are developing heavily in oil will bring a great many things in there to be done on the spot for the service of the oil industry.

MR FRAWLEY: Like what?

A. All that must be done for the service of the drilling section of the oil industry.

Q. Those things all come from Oklahoma, don't they?

A. Well, no doubt they do immediately after you begin. What I am trying to do is to look forward for let us say not more than ten years. Are there not signs already that it is developing?

Q. I have been down here on freight rate cases so long that I don't know.

A. I must say, all I have got to go on is from the reports I read of people locating branches in Edmonton and

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in Calgary. I have not been there recently.

THE CHAIRMAN: Then I think you were saying that Alberta has become or is about to become an industrial part of Canada, and then I interrupted you. What were you saying from that? What was the result?

A. Well, the very fact that Alberta is so rich in other things may make it a little bit harder to develop industry. If wages were lower in Alberta I would see an industrial development coming much more quickly. But just because they have oil and gas I think that many things are going to come in there in the next, as I say, ten to fifteen years.

Q. How do you relate that to the transportation problem?

A. Well, what I am saying is that if Alberta would measure itself against what it was twenty-five years ago and not against areas whose development began earlier and which are also in a different geographic setting, the resulting attitude would probably be sharply different from what it now is; and, certainly, for any understanding and measurement of the process of growth, the bench-mark must be Alberta as it was at some past point of time, and not what some other area is now.

MR EVANS: Q. When you speak of attitude, you are speaking of Alberta's attitude in regard to freight rates?

A. Yes.

Q. Now, as I understand it, the Alberta brief has as its thesis that relative rates as between raw and finished goods should either be passive or should encourage processing at or near the point of raw material production. What do you say about that?

A. Well, I think it is probable, though it is by no means certain, that such a rate structure might, for a time, encourage a more rapid rate of industrial development in

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...and I will be glad to enter his name

Alberta. That seems to be the reason why it is put forward. But the rate structures of railways serving the whole nation must be national in their form and purposes.

I believe that there are two major principles here which are mutually exclusive. One can attempt to use the rate structure in order to produce a particular type of economy. Such a rate structure is an integral part of an all-inclusive national plan. Alternatively one can attempt to have a rate structure which is economic in its intent.

Q. Would you explain what you mean in distinguishing between a plan which is an all-inclusive national plan and one which is economic in intent?

A. Well, in the all-inclusive plan there is some group which not only plans but which has the power to enforce its plan. They set up what they want to do, trying as best they can to gauge their plan against the available resources, and consumers have the end products of the plan for consumption. An economic plan is one in which people are allowed to express their demands freely through prices, and in which ultimately what is produced is a reflection of what consumers want.

Q. Would you like to develop that a little further, perhaps?

A. Well, I might say that in a planned economy there is no room for an economic calculation, in the sense that if the ultimate product is determined by the plan, then people take what they can get; they do not make that individual distribution of their incomes to produce those things which they most want.

Q. How would you add to your description of a rate structure that is economic in its nature?

A. Well, an economic rate structure is one which offers

rates at which traffic will move and which will result in adequate earnings to the railways which move it. Instead of putting the railways (or the regulating commission) in the position of deciding what shall and what shall not be done, it leaves the initiative to the rest of the community. The railways are relatively passive. They make such rates as will develop traffic, but they do not take upon themselves the responsibility of developing any particular type of economy. Indeed, if they are open to any serious criticism, it is that they have been a shade too passive in their response to a radical worsening in the condition of declining industries and have frequently tried to keep them alive by rate reductions when it might have been wiser to let them cease.

Q. Now I might go to a somewhat different subject---

COMMISSIONER INNIS: Q. When you talk about planned economy, do I infer that you are inclined to draw a sharp distinction between what we think of as our present society and a planned society?

A. Not between our present society and a planned society. I think of what we now do as being a halfway house which is not permanently tenable, that we can either go back to a free society or we will be inevitably pushed forward to a wholly planned society.

Q. I am afraid you have missed my point. Let us take the Canadian Pacific or the Canadian National; they are large, powerful organizations; I suppose that they have plans for the next ten years or five years?

A. Yes.

Q. As to what they intend to do. You do not regard that as a planned---

A. It is definitely not an over-all plan; and, secondly, are they not rather expressions of hope? I see, for

example, that you have a determination to build the Trans-Canada Highway and to contribute by the Dominion toward that building.

Q. Yes; well, does that type of planning---

A. May I continue, sir? I do not see any kind of relationship between that and the capital needs of the railways over the next five years, and yet I think that in net production to the community the spending of the same amount of money upon the railways would produce a greater volume of useful goods than any spending on the Trans-Canada Highway.

Q. Again, the Trans-Canada Highway is another illustration of planning, and I am just wondering whether you are deliberately overlooking the extent to which large organizations have planned for the next five or ten years in your contrast?

A. I wonder, sir, if you would not say that the Trans-Canada Highway is rather planned against the community than planning for it.

THE CHAIRMAN: Q. Is rather what?

A. Planning against the community rather than planning for it.

COMMISSIONER INNIS: I am not arguing whether it is a good thing or a bad thing; I am simply arguing that this is the proposed outlay, in which resources will be attracted to that particular development?

A. It is a proposed outlay which is not subject to any price test.

THE CHAIRMAN: Q. Is not which?

A. Is not subject to any price test. Nobody has to justify the expenditure of the money by what it is going to produce in net benefit to the Canadian community.

MR EVANS: I am wondering if Dr. Innis did not

perhaps intend to ask you to distinguish between planning from the top for the whole economy and individual planning by corporations. Was that the thought you had in mind?

COMMISSIONER INNIS: Well, I was a little bit worried about Professor McDougall's reference to rather large vague phrases like totalitarianism so on, which always set me on my guard, and the same is true of planning -- whether that is perhaps not overlooking the actual situation.

THE WITNESS: Obviously, sir, everybody must plan for his own particular activities, yes. He gets as far as he can with his plans in the social medium in which he finds himself. But when you come to planning on a national scale, then there is equally room for carrying out those who might interfere with the realization of it.

THE CHAIRMAN: Q. Don't you think a large railway like the Canadian Pacific plans on a national scale? It must, mustn't it?

A. It plans its particular response to what it thinks the behaviour of all the rest of the economy is going to be. Now, that falls very far short of planning over Canada.

Q. And territorially throughout the whole country?

A. And territorially, oh, yes.

COMMISSIONER INNIS: Mr. Evans, surely if they are planning in relation to C.P.R. profits, that is still---

MR EVANS: Well, I don't know that I said they were planning as regards profits. I suppose Mr. McDougall's word would be better -- we are hoping.

COMMISSIONER INNIS: Well, you did not like to be put in the general position in which your interests were entirely eleemosynary.

MR EVANS: Oh, no. I think I would be quite unrealistic if I did not say we were---

MR MACPHERSON: We heard from Mr. Newman about the five-year plan.

MR EVANS: Yes; you remember Mr. Newman said that plan represented what they thought was necessary, but it must not be called a programme in the sense that it is a commitment to undertake it.

THE CHAIRMAN: Well, we can think it out through the night.

---The Commission adjourned at 4:48 p.m., to meet again at 10:30 a.m. on Tuesday, March 14, 1950.

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ON
TRANSPORTATION

EVIDENCE HEARD ON

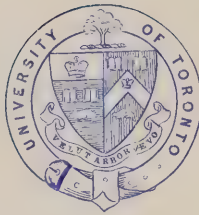
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ROYAL COMMISSION ON TRANSPORTATION

Tuesday, March 14th, 1950

Index Page #114

	<u>Page</u>
<u>EXHIBIT No. 205:</u> Report from Montreal Gazette of March 14, 1950, re Canadian Pacific's 1949 operations. (Filed by Mr. Frawley) - - - - -	17911
<u>EXHIBIT No. 206:</u> C.P.R. Estimated Impact on Freight rates of an allowance of an 8.2% rate of return. (Filed by Mr. MacPherson) - - - - -	17911
<u>EXHIBIT No. 207:</u> C.P.R. amount Available to Ordinary stockholders from the Allowance of an 8.2% Rate of Return. (Filed by Mr. MacPherson) - - - - -	17911
<u>PROFESSOR J. L. McDOUGALL</u> - Recalled. Examination by Mr. Evans continued - - -	17912
Examined by Mr. Covert - - - - -	17926
Noon adjournment - - - - -	17978
<u>PROFESSOR J. L. McDOUGALL</u> - Recalled. Examination by Mr. Covert continued - - -	17979
<u>P. C. ARMSTRONG</u> - Called. Examined by Mr. Sinclair - - -	18037
Adjournment - - - - -	18044

- - - - -

ROYAL COMMISSION ON TRANSPORTATION

OTTAWA, ONTARIO
TUESDAY
MARCH 14, 1950.

THE HONOURABLE W.F.A. TURGEON, K.C., LL.D. - CHAIRMAN
HAROLD ADAMS INNIS - COMMISSIONER
HENRY FORBES ANGUS - COMMISSIONER

G.R. Hunter
Secretary

P.L. Belcourt
Asst. Secretary

COUNSEL APPEARING:-

F.M. Covert, K.C.	}	Royal Commission on Transportation
G.C. Desmarais, K.C.		
H.E. O'Donnell, K.C.	}	Canadian National Railways
H.C. Friel, K.C.		
F.C.S. Evans, K.C.	}	Canadian Pacific Railway
I.D. Sinclair		
C.D. Shepard	)	Province of Manitoba
M.A. MacPherson, K.C.	)	Province of Saskatchewan
J.J. Frawley, K.C.	)	Province of Alberta
F.D. Smith, K.C.	}	Province of Nova Scotia; Transportation Commission of the Maritime Board of Trade
J. Paul Barry		
C.W. Brazier		
J.O.C. Campbell, K.C.		
	)	Province of New Brunswick
	)	Province of British Columbia
	)	Province of Prince Edward Island.

Ottawa, Ontario
Tuesday, March 14, 1950.

M O R N I N G S E S S I O N

--- The Commission resumed at 10.30 a.m.

THE CHAIRMAN: Very well, Mr. Evans.

MR. FRAWLEY: Before Mr. EVans proceeds with his examination, Mr. Chairman, I thought that it might be proper for me to offer as an exhibit the Canadian Pacific's annual report which was released to the press yesterday afternoon. I call it the annual report. I mean that it is the heart of the operating results of the Canadian Pacific for 1949. The headline reads, "Canadian Pacific's gross, net higher; 'other income' remains big factor." Net income for 1949, my lord, was \$29,724,000. In 1948 it was \$27,393,000. In 1947 it was higher; it was \$31,893,000. In 1946 it was \$25,134,000. Then comparative figures are also given in the newspaper report. It is hardly a newspaper report. The opening paragraph reads:

" Preliminary figures on results of operations during 1949 of the Canadian Pacific Railway Company released here"-- that is in Montreal -- "yesterday afternoon following a meeting of the directorate, show a further increase to a new record in gross earnings and net income which was substantially better than in 1948."

I do not want to interrupt or take any more time with it than that, but I would like to offer it as an exhibit.

MR. EVANS: I have no objection to that going in. I do not know whether it is accurate or not. It is a newspaper report. There will be, I should think, before the Commission finally closes its hearings the official annual report of the Company. I have no doubt that the figures are accurately reported.

MR. COVERT: It will be Exhibit 205.

EXHIBIT NO. 205: Report from Montreal Gazette of March 14, 1950, re Canadian Pacific's 1949 operations.

MR. MACPHERSON: The other day I referred to exhibits that had been filed in the 20% case during the evidence of Dr. Dorau. Those exhibits were 49-92 and 49-93. They showed the effect of the 8.2% rate of return on the rate base obtained by the C.P.R. of \$1,001,000,000. I now propose to file these two exhibits from the 20% case as Exhibit 206.

MR. COVERT: Did you say there are two?

MR. MACPHERSON: There are two sheets.

THE CHAIRMAN: They are going in together?

MR. MACPHERSON: I will file them as one exhibit.

THE CHAIRMAN: Will they be one exhibit or two?

MR. COVERT: I am just going to look at them. It might be better to file them as two exhibits. 206 will be Canadian Pacific Railway estimated impact on freight rates of an allowance of an 8.2% rate of return, and Exhibit 207 will be Canadian Pacific Railway Company, amount available to ordinary stockholders from the allowance of an 8.2% rate of return.

EXHIBIT NO. 206: C.P.R., Estimated Impact on Freight Rates of an Allowance of an 8.2% Rate of Return.

EXHIBIT NO. 207: C.P.R., amount Available to Ordinary Stockholders From the Allowance of an 8.2% Rate of Return.

MR. EVANS: I do not know what my friend thinks he proves by that because Canadian Pacific is not asking this Commission nor did it make any application to the Board based on an 8.2% return. I think my friend is perhaps trying to create the atmosphere that what we are asking for is something staggering.

THE CHAIRMAN: Perhaps we had better ask Mr. MacPherson what he is leading to.

MR. MACPHERSON: Dr. Dorau's evidence --

THE CHAIRMAN: Dr. who?

MR. MACPHERSON: Dr. Dorau's evidence in the 20% case has been referred to from time to time during this hearing, and it has been referred to, as a matter of fact, during the course of the examination of the present witness. These are filed as indicating the effect on freight rates in this country. One exhibit establishes that the increase in rates would be 81% above the rate before the first increase went into effect.

THE CHAIRMAN: All right; go on.

PROFESSOR J. L. McDOUGALL - RECALLED

EXAMINATION BY MR. EVANS(Cont'd):

Q. Mr. McDougall, at page 141 of part 2 of the Canadian Pacific brief the statement is made that the freight charges are borne by the consumer. Do you agree with that?

A. Yes, sir, I do. It is clear that this must be the case under normal conditions. In general consumers pay the total cost of production because they buy the goods. When a man buys a loaf of bread he has paid all the costs of producing that bread. Now admittedly this is not true to the extent to which at any time any of the agents of production accepts an actual loss on his operations - that is, he spends more money in order to produce his share of the loaf than he receives in return. I am, of course, allowing for such long term costs as are represented by depreciation.

Q. What is the protection against the weakest agent being forced to accept --

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A. I think the only protection the weakest producing agent has against being forced to accept a labour income of zero is the fact that at some point he will cease to function.

Q. You mean cease to function as --

A. As a producer.

THE CHAIRMAN: Q. I did not hear that.

A. He will cease to function as a producer. That is his ultimate and a severe limitation but still a very clear limitation.

MR. EVANS: Q. That is, if the producer's income sinks to zero then he ceases to be a producer??

A. Yes, I would think even when it sinks towards zero that process of moving out of that particular line of production will start.

Q. Yes.

A. That means that even in times of depression the consumer will benefit from all cost reductions up to the point where he ceases to obtain a supply of goods.

Q. Yes.

A. I argue that in good times or bad all costs of production will be paid by the consumer so long as production and consumption are continuing. What I am trying to say is that the interests of any producer are going to be protected out of general market conditions which enable him to receive a remunerative price from the consumer and not out of any special reductions in this or that individual cost of production; that wheat growers, for example, are not going to be saved from disaster in a generally adverse situation by reductions in individual items of cost.

They will prosper when there is a good market for wheat and when their crops are good, but they can never prosper out of reducing costs of production, that those reductions in this depressed situation will go to the consumers, that

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there is no salvation to be found for producers --

THE CHAIRMAN: Q. No what?

A. There is no salvation to be found for producers in whittling freight rates downward.

MR. EVANS: Q. Now then, it is your view that consumers must in the end bear freight rates and that in periods of prosperity it is quite easy to pass these costs on to the consumer. When the Canadian Pacific studied changes in the national index of the cost of living according to its brief it was not able to discover any sign of increased freight rates being passed on after April, 1948. How do you account for this?

A. Well, I think, sir, it is not too difficult. First of all, as I have said yesterday, your rail freight and switching revenue is a relatively small part of the gross national product - at 1947 4.5%. Since many if not most of the commodities entering into the cost of living are relatively high value goods it is probable that freight costs are an even lower percentage of their value.

Q. When you speak of lower you mean lower than that average of 4.5?

A. Yes. Secondly, the normal merchandising margins are bigger than the transport costs. In periods of prosperity they tend to grow wider still. Minor increases in cost - and the freight rate increase of April, 1948 was just that -- are quite often absorbed under such a condition. I am quite prepared to admit that the increase in freight rates might at that time have had some influence on the cost of living but I am not in the least surprised that it was too small to be demonstrated. This is merely another proof that railway revenues are a very small part of the gross national product.

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Q. Does the study of the changes in the index of the cost of living which is set out in the brief in the eight cities that the study deals with bear out that view?

A. Yes, sir, I think it does. The only city in which there is any significant movement out of line is in Vancouver, and it is a case that might merit special study to see whether the increase which took place was actually due to the increase in freight rates or was due to a further widening in the distribution margin. I think I must point out that when the whole population is conditioned to accept substantial rises in prices when freight rates rise merchants are under substantial temptation to increase their margin of net profit on sales, and to allow the railways to absorb the odium arising from the change in prices.

Q. Now then, the brief contains a special set of studies on particular commodities. Do the studies with regard to particular commodities set out in that portion of the brief support what you have said about the more generalized index of the cost of living?

A. Yes, sir, I think they do. In relation to items like men's shoes or men's suits there was no connection between the retail price and the amount of transportation charged from the manufacturer to the retail store. For example, lower prices were quoted on men's shoes in British Columbia than within 100 miles of the factory in New Brunswick.

Q. There was also the example of a carpet, was there not?

A. Yes. We got prices on carpets of various sizes. You might take the 9 by 12 as an example. They sold anywhere from \$87.50 to \$115.50 in various markets across

1917-1918

Canada, but the highest prices did not coincide with the highest transportation cost from the factory,

(Page 17917 follows)

and the spread in prices between retail outlets was about six times as great as the maximum transportation cost from the factory.

COMMISSIONER INNIS: Are those prices from Eaton's catalogue?

A. Well, this was a branded line so, short of bringing in a carpet man we could not get a comparable item out of Eaton's catalogue to match against the brand.

COMMISSIONER INNIS: Q. Eaton's catalogue would ^{tend} to set a level of prices in all commodities handled by Eatons?

A. Oh, yes, but even if the same manufacturer manufactured that carpet and sold it to Eatons on the same specification it would be an Eatonia or a Glen Eaton carpet, it would not be a Sea Shore, a brand name.

Q. I merely wonder how far the whole principle of a fixed price across Canada would tend to determine the prices of the sort of commodities you have suggested.

A. But on this particular carpet you had a range of \$87.50 to \$115.50.

THE CHAIRMAN: Is there a range of prices in the catalogue? ^{A.} There are different prices on carpets of different qualities. ^{Q.} I mean for the same carpet?

A. For the same carpet.

Q. It would be the same price all over in the catalogue?

A. It would be the same price in each area in which that particular catalogue circulated. Now, I am not completely confident that the same catalogue is distributed nationwide.

COMMISSIONER INNIS: Q. The main problem is that you are dealing with the sort of commodity which lends

itself to that type of price.

A. Well, we took the advice, almost shall I say, the direction of the Bureau as to what commodities you could get on a national basis. For very obvious reasons. A study made between June and September could not take in potatoes because there is no national distribution of potatoes in any real meaningful sense, and what would you do between new crop and old crop potatoes and so on even in any one town? You had to pick things which had a national market and which were identifiable, so that you took a relatively good grade of shoe; it might well be that you might have had more or less variation on lower quality sold in different fashions, but I think we got that fairly well in the study of men's suits, because there we had in that one case as a standard things sold under a given brand name across Canada and in the other we had a men's suit which was sold f.o.b. factory and then thereafter the retailer was entirely on his own, and I must say sometimes he did strange things.

THE CHAIRMAN: Q. Did he pay the freight rates?

A. Oh, yes, on the second men's suit the retail merchant paid the shipping charges, he set his own price, everything was in his own hands, whereas with the first case the firm in Toronto which produced that suit had its own outlets, had agents whose prices they controlled and so on.

MR. EVANS: Q. Now that you have mentioned the matter of suits, this suit that was sold f.o.b. factory -- what result did you find when it came to an attempt to measure the effect of transportation increases and costs on the retail price of that suit?

A. Well, on that particular men's suit I will give the

price at June 1 only.

Q. Which is the retail price?

A. The retail price. Now, in Moncton, \$52.50 and \$54.50; in Sydney, \$58.00 and \$57.50; in Yarmouth, Truro, and Edmundston, \$57.50; Belleville Ontario, \$55.00, \$55.00 and \$57.50; Fort William \$57.50; Regina, \$60.00; Lethbridge \$55.00 and \$55.00; Calgary, \$55.00 \$55.00 and \$59.00; Edmonton, \$52.00, \$57.50, and \$61.00; Trail, B.C., \$57.50, \$54.00, \$55.00; Nanaimo, \$57.00, \$57.50, and \$59.50.

Q. Where was that suit manufactured?

A. In Montreal and at a price f.o.b. factory of \$35.00.

Q. Was there a Montreal price included in your list?

A. No, the difficulty was that you could make a reasonable check on a small market like Belleville, Ontario or Kingston, but if you are going to check on the outlets to get a representative price in Montreal alone you would be compelled to put in something close to a month and there was not that much time.

Q. Now, out of all the listed prices you have just referred to, where was the lowest price obtained and where was the highest price obtained?

A. I think the \$52.00 in Edmonton was the lowest.

MR. FRAWLEY: Q. Did that move on a class rate or on a commodity rate?

A. Men's suits go by express, indeed, they will use air freight for suits very frequently although when they ship air freight they will ask the customer to pay the difference between the rail express and the air freight.

And Edmonton also had the highest price at \$61.00.

Q. The same suit?

A. The same suit, different store.

Q. Different street?

A. Different street, different kind of service, maybe a different store front.

Q. East of First Street or West of First Street?

A. Could be.

MR. EVANS: Q. Now, you have been giving us something of what you might call the high grade commodities. Does what you have found apply to low grade commodities or low-value commodities?

A. Well, it does to a degree, to an almost surprising degree. I had expected in relation to the low-valued commodity that the freight rate would be a much more decisive factor in price setting than in fact it was, but we got prices on Portland cement and we found that the differences in dealers' margins were more important than the increase in freight charges at April, 1948.

Q. Now, would you sum that up a little?

A. If I may sum up this whole section, - and it is really too large to put in, - transportation is merely one small part of the total cost of getting goods from the point of production into the hands of ultimate consumers. It has been given a much greater importance in public discussion than the facts warrant. The community gets transportation services from the railways very cheaply. It has far more to gain by encouraging technical development ^{and correlative cost reductions by} / the railways than by trying to reduce railway earnings below a reasonable level.

Q. Perhaps I should have asked you before we dealt with this, what connection you have had with the study we are talking about?

A. Well, the students were engaged on my recommendation, they reported to myself and to Mr. Armstrong, and they were given a completely free hand because we had not enough time to direct them, if for no other reason. They spent about a month at Ottawa with the Bureau and with the Wartime Prices and Trade Board and anybody else they could find. They made up their list of commodities upon their own, and they were sent out across the country, there were two of them. They brought in their material and wrote it up themselves.

MR. EVANS: Thank you Mr. McDougall.

THE CHAIRMAN: Does anyone wish to examine?

MR. COVERT: Mr. Chairman, I asked Mr. MacPherson, Mr. Shepard, Mr. Smith, Mr. Brazier, Mr. Frawley, Mr. Friel, and they all said they had no questions, but I think Mr. MacPherson said he had a statement to make.

MR. MACPHERSON: I just have to say this: insofar as the witness asserts the position that the railway occupies in the transportation economy of the country I certainly agree entirely.

THE CHAIRMAN: What?

MR. MACPHERSON: Insofar as the witness asserts the position that the railway occupies in the transportation economy of the country I certainly agree entirely, but insofar as his other views are concerned I think they have been subject to cross-examination from time to time and in the light of the fact, as he has said, as he said yesterday, the proposals of the C.P.R. were too modest, then I think that to pursue cross-examination would simply be inviting interminable argument and this is the ninety-fifth day of the sittings.

THE CHAIRMAN: I am reminded that your submission for the province of Saskatchewan on page 88 raises the question that Professor McDougall dealt with yesterday,

of
that/a possible government ownership of Canada's railway
system. Your brief reads:

" Further to the question of competition in
the transportation field the attention of the
Commission is drawn to page 7 of the Saskatchewan
Outline of Representations. It is there suggested
that a study of the possible contribution which
public ownership of all railways could make to
the solution of Canadian transportation problems
might well be undertaken."

That is as far as your brief goes.

I remember asking you some time ago whether
you intended to adduce any evidence.

MR. MACPHERSON: Nothing further.

THE CHAIRMAN: So far as I recollect Mr.
McDougall is the first one who has raised this in the
course of the evidence and since your provincial government
is interested in the question I was wondering whether
you would like to ask him any questions?

MR. MACPHERSON: Nothing that I do not propose
to deal with in argument, my lord.

MR. SHEPARD: I think I would say that I
associate myself with Mr. MacPherson's comments as to
why he is not proposing to cross-examine Professor
McDougall. Manitoba shares those views. I am not
instructed to cross-examine, -- in fact I am instructed
not to cross-examine him simply because the matters that
he dealt with that are germane to our submission we have
already discussed with other witnesses in cross-examination
and some of his other remarks I feel can be just as well
disposed of in argument.

THE CHAIRMAN: Is counsel for Prince Edward Island here?

MR. COVERT: No, sir.

MR. BRAZIER: I would like to associate myself with the remarks made by Mr. MacPherson and Mr. Shepard. I am speaking on behalf of British Columbia.

THE CHAIRMAN: I asked about Prince Edward Island because that province devotes a very large part of its brief to the discussion of government ownership of Canada's railway system.

MR. EVANS: May I just put in one word about the matter of amendments? The only ones that I have received are those given to me by Mr. Shepard. I do not want to interject a note of complaint but our case is drawing to a close and I would like very much to have those in my hands before that time.

THE CHAIRMAN: I thought you had received some from Mr. Frawley a long time ago?

MR. EVANS: Well, he has taken them back for revision, if you will remember. He said to your lordship some weeks ago that he had some prepared then, but he had not them all prepared, and he has yet to produce them.

MR. FRAWLEY: I really appreciated^{it}/when my learned friend rose that he was directing himself to me. I have said that I have a considerable number of amendments that I have thought were required to properly establish the proposal I was making and I assure your lordship we have not been indifferent to the situation, we have, on the contrary, been very diligent, and we have nearly all our amendments now in shape to offer, and I think it will be a matter of days. I had hoped to be able to deliver them

to the Commission and to my friend before his case actually closed. I think if Mr. Armstrong is going to be any appreciable time, it will only be a matter of days before I get the amendments in.

I want to associate myself with what my friends of the provinces have said with regard to the cross-examination of Professor McDougall. I challenge what he has said insofar as it bears at all upon any of the proposals that I have made. Perhaps, with too much confidence, I think he has done my case no harm. I do not propose to cross-examine him.

(Page 17926 follows)

EXAMINED BY MR COVERT:

Q. Now, Professor McDougall, my understanding is that you believe that, since the statistics in 1947 indicated that approximately only 4.5 per cent of the total -- was it the total value of the goods?

A. Gross national product, yes.

Q. Gross national product, was taken up in freight rates---

THE CHAIRMAN: What is the percentage again?

MR COVERT: 4.5 per cent.

Q. That in effect freight rates do not play a major role -- that is, freight rates as of themselves do not play a major role -- in the economy, and that an increase, for instance, of the nature of 40 per cent on that 4.5 really would not affect people very greatly?

A. Well, first of all, remember that the 4.5 is a weighted average for the whole community; there will therefore be places where it is more important and others where it is less.

Q. But, as I say, in general you use those statistics to show that?

A. Well, as a broad average demonstration, yes. Secondly, as to the importance of a 40 per cent increase in freight rates, the question is, against what kind of environment does that increase take place? A 40 per cent increase in freight rates when the price level is completely stable is a totally different thing from a 40 per cent increase in freight rates when wholesale prices have upon the average more than doubled.

Q. Well, you say, I take it, that in the case where they have more than doubled that 40 per cent increase would not have much effect?

A. It would have a relatively small effect, yes.

Now, the exact effect will depend rather more upon timing than upon amount.

Q. Now, as I say, subject to the explanations you have just made, you would agree with the proposition that I put to you?

A. Yes.

Q. Now, that 4.5 per cent, as far as that is concerned, that may have changed a bit following the increases?

A. Oh, it might have risen by as much as .1.

Q. You mean by that, it would be something like 4.6?

A. 4.6, 4.65. You see, there was about a 10 per cent increase in gross national product in that same period -- yes, a gross national product at 1947 of 13,591 million, and in 1948 the preliminary figure is 15,450 million, so that both sides of that equation are changing. It might be less than the .15 that I put as the outside limit.

MR EVANS: Q. What was the first year you gave?

A. 1947.

MR COVERT: Q. Now, you would agree, Professor McDougall, that it does make a great deal of difference in taking the percentage as to whether it is a high-valued or a low-valued commodity?

A. Oh, yes, but it is subject to the particular example of cement which I have just quoted, where the change in the dealer's margin was more important than the change in the freight rate, and even at points very considerable distances from the point of origin.

Q. What I mean, Professor McDougall, is this, that the percentage does vary?

A. Yes; it is an average, and therefore there are variations about the average.

Q. And perhaps it is a dangerous figure to use because it is an average?

A. A weighted average cannot be dangerous. If it were an unweighted average I might agree.

Q. You say a weighted average cannot be dangerous?

A. Unless you offer positive proof of a very wide standard of deviation.

Q. That is your view?

A. Yes.

Q. Now, have you examined any of the American studies dealing with the ratio of freight rates to the wholesale prices that were made in the year 1941?

A. Are those the ones that are quoted in Locklin?

Q. Yes.

A. I have looked at them, yes.

Q. You have seen, for instance, that the freight rate to the wholesale price varies from as low as 1.2 per cent to as high as 50.9?

A. Yes.

Q. Depending on the particular commodity?

A. Yes.

Q. And that, for example, in the case of vegetables they varied from as low as 12 per cent to 75 per cent?

A. Yes.

Q. Have you had an opportunity, doctor, to study the report made by the Wartime Prices and Trade Board in 1946, which dealt with the ratio, I think it was, of freight rate to the price in the case of hauls of under 400 miles, and then from 400 to 1,000 and from 1,000 up?

A. I do not recall it; I do not believe I saw it.

Q. Take the case of one example, canned peas, for example, where they show that the freight rate was 4.38 per cent of the price on the 400-mile haul, nearly 16 per cent when it was between 400 and 1,000, and 18.36 when it was over 1,000?

A. Yes.

Q. Now, I think that perhaps would clearly indicate that the freight rate does vary a great deal as a ratio of the price of the product?

A. Now, this percentage you quote, it was a percentage of the factory price or of the final retail price?

Q. I think it was of the f.o.b. price at the factory. I will check that. It was the price f.o.b. at the point of origin.

A. Yes.

Q. It says :

"In order to achieve comparability and to eliminate the influence of the freight rate itself on the percentage."

A. It is a demonstration---

THE CHAIRMAN: What were the words? I did not hear you.

MR COVERT: "In order to eliminate the influence of the freight rate itself on the percentage."

Q. I just wanted to ask you, doctor, if it does not indicate that freight rates in themselves as a ratio of the price vary to a great extent, depending on the commodity, and also on the length of haul; you would agree with that?

A. Yes. This is a country of regional specialization. If you are going to haul things long distances, the things that get hauled long distances are going to involve heavier transportation costs than those involving short, yes.

Q. Are you quite finished?

A. Yes.

MR EVANS: I am going to object to that kind of attitude to the witness.

MR COVERT: What is the objection?

MR EVANS: You turn around, walk away from him

and come back with a snarl on your lips, and you say, "Are you finished?" Now, that is not fair.

MR COVERT: Are you addressing me?

MR EVANS: I am objecting to Mr. Covert's conduct to the Commission.

THE CHAIRMAN: Go on, Mr. Covert.

MR COVERT: Is your objection made to the Commission?

MR EVANS: Yes, it is.

MR COVERT: Then I will address myself to the Commission.

Mr. Chairman, I thought that the answer itself of Professor McDougall was finished, as far as I was concerned; he had given me the information, and it seemed to me that he added some material which I was not interested in, and I think perhaps we can shorten the thing if he will answer my questions and leave it at that. If he wants to add something else, that is his privilege. As far as the "snarl on my lips"---

THE CHAIRMAN: As a general rule of procedure I think that is right, provided the witness, of course, is not compelled to answer always by Yes or No, if there is a qualification to follow properly. I understand.

MR COVERT: Q. Now, I think perhaps, Professor McDougall, you would also agree that there are many considerations -- that is, for example, the value of the product itself, whether it is high rated, a high-valued commodity or a low-valued commodity, whether it is heavy or light; the percentage of the freight to the value changes with those conditions?

A. Considerations in what respect?

Q. Well, perhaps I will make it a little clearer. If you are shipping shall we say logs a long distance or a

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short distance---

THE CHAIRMAN: What do you say?

MR COVERT: Q. Shipping logs a long distance or a short distance, that the percentage of the freight rate to the value of that commodity may vary quite a bit?

A. Oh, yes.

Q. Also if it is a can of peas for a long distance or a short distance?

A. Yes.

Q. And then, comparing the peas with the logs, it changes a great deal?

A. Oh, yes.

Q. In other words, the percentages of freight to cost vary a great deal, tremendously, as a matter of fact, from a fraction of one per cent to as high as over 70 per cent?

A. In particular cases.

Q. That is right.

A. All I am saying is that when you take a grand average you come out to 4.5, and it is a weighted average.

Q. Now, I was not sure this morning that I did get your answer to a question put by Mr. Evans, but it did seem to me that it was to this effect, that generally speaking because freight rates as a whole were of such a small amount in the price, such a small proportion of the price, in general they did not have a great effect, and that all the complaints that we have heard are really overstated?

A. In relation to the index of the cost of living, certainly. I stand by that absolutely.

Q. Now, I just want to read to you, Professor McDougall, a short statement from one of the judgments before the Interstate Commerce Commission.

A. It would be easier, Mr. Covert, if I could see it

also. Are there two copies?

Q. It is in volume 84. I will show it to you, Professor McDougall. I have not the case before me, my lord, but there is a quotation from Ex Parte 162, and I think it was at page 614. At the time they were handing down the decision involving roughly I think a 20 per cent increase. It is on page 16466 of the record. They say there:

"We therefore pass to our ultimate findings. Before stating them we think the following observations should be made. There are here involved all freight rates and charges, and all passenger fares on railways and many other carriers of the nation, large and small. What we do will directly affect production and distribution in the industries of the nation, and the welfare of those various regions, as well as the transport industry. It will have its effect on the forces tending to economic stabilization or the reverse. We have accorded every reasonable opportunity for those in any way affected to be heard, while pressing the proceeding with as much speed as the size and complexity and detail of the proposals permitted. No case has ever received from us more earnest study."

Now, I think that was a quotation from a previous case, but it was apparently applied at this time with approval, or cited with approval, and it seems to indicate that in the view of the Commission they felt that a case of this kind had that effect, in other words:

"What we do will directly affect production and distribution in the industries of the nation, and the welfare of those various regions, as well as the transport industry."

Now, it seems to me that that is an indication at least that in their view an increase of this kind had a tremendous effect.

A. Well, this case was decided December 5, 1946.

Q. That is right.

A. Now, the facts since do not bear them out, because if they were expecting an adverse effect upon production, it did not occur.

Q. Well, now, just a minute, Mr. McDougall. I do not say that this says that it would have an adverse effect---

THE CHAIRMAN: Was not that what they were trying to avoid?

MR COVERT: Exactly.

THE WITNESS: They were trying to avoid it.

MR COVERT: Yes.

THE WITNESS: Increases were given.

MR COVERT: Yes.

THE WITNESS: And there was a very sharp increase in the index of industrial production. I have it here. In 1946, 170 -- this is on a 1935-39 base -- in 1947, 187; in 1948, 192.

MR COVERT: Q. Could we just get down to this: Would you say, Professor McDougall, that they were wrong when they just made the statement, "What we do will directly affect production and distribution in the industries of the nation"? You think they were wrong?

A. No, I do not, because anything that anybody does has some effect, and the larger the body operating the greater its effect. But I would say first of all that the railways were not big enough of themselves to have a decisive effect upon the development of the level of production, and I would say secondly that the attempt to fight an inflation on a freight-rate basis rather than on a

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central banking basis is obviously silly.

Q. Professor McDougall, you feel, for instance, that a 40 per cent increase in freight rates over and above what it was at the end of the war---

A. Well, it is the same at the end as at the beginning; we might as well start from where it begins.

Q. All right. I just made a calculation, 21, and 16 per cent on top of that would bring it up to about 140?

A. Yes.

Q. You say as far as 40 per cent is concerned, that would not effect many people adversely?

A. I should say this, that for anybody who had an average increase in his selling prices which comes close to the 100 per cent -- I should say, rather, more than the 100 per cent -- an increase of 40 per cent in freight rates means that he is better off now than he was at 1939. Now, obviously if you have people whose price increase fell below 40 per cent above 1939, they are going to be worse off, but I would like to see them identified first.

Q. You would not think there would be many of those?

A. No; I do not know of any case of that kind.

Q. Now, carrying the 40 say to 80, what would you say?

A. It would be more important.

Q. It would be more important?

A. And if you have had any expansion of production based on the idea that it was possible to hold freight rates at a 1939 level while doing business on the new higher post-war price level, then that particular operation might get badly pinched, yes.

Q. But is there any relation to the amount that you can go as far as increases in freight are concerned, and the amount that the prices or other costs generally have gone up, in your opinion? I just wanted to find that out.

A. Well, I do not regard the regulation of freight rates as being keyed to the wholesale price, if that is what you mean.

Q. No, I do not mean that, Professor McDougall, at all. For instance, if prices generally went up 100 per cent, that would not mean that freight rates could go up 100 per cent?

A. It need not necessarily mean that, no.

Q. But it could?

A. It is possible.

Q. In other words, could we put it this way, that freight rates could go up just as much as other expenses? For instance, if other expenses went up 100 per cent, perhaps freight rates should go up 100 per cent too?

A. Would you define other expenses?

Q. Well, costs of production.

A. In railways or in industry, which?

Q. In industries.

A. Well, I would rather think in terms of the increase in cost in railway production, because it need not be the same as an industry generally.

Q. No, but then on the other hand if costs of the railway went up 100 per cent, that would not mean that the freight rates should go up 100 per cent -- or would it?

A. Well, I would want to know why it should not.

COMMISSIONER ANGUS: Q. Are you thinking of operating costs or over-all costs?

A. If Mr. Covert will define, I can start, but until he defines I cannot.

MR COVERT: Q. Let us take over-all costs.

A. If over-all costs have gone up by 100 per cent, and if all prices in industry have gone up by 100 per cent, then I would think it not improper that railway rates should

equally go up by 100 per cent.

Q. Now, you would think it possible that there may be some relation then between the percentage of increases in freight rates to the percentage increases in costs? All I am trying to find out is if there is any relationship; I think that is the question I---

A. I would think so; subject to qualification, but generally speaking, yes.

Q. You would recognize, Professor McDougall, that you could have a tremendous increase in, for instance, operating costs, and no increase required at all in freight rates?

A. Well, if I could understand how you square your accounts I could feel happier in answering.

Q. You cannot envisage that?

A. I cannot envisage -- if you start from a relatively normal situation, if you have an enormous increase in costs and no increase in rates, then who bears the loss?

Q. Well, is there necessarily a loss?

A. The expectation is that there will be.

THE CHAIRMAN: Q. There will be what? Would you please turn this way?

A. Sorry, sir.

Q. What is it you say?

A. I thought that Mr. Covert was envisaging a situation in which there was a very great increase in cost.

MR COVERT: Q. That is, operating cost.

A. Yes, operating cost; and there was no increase whatever in the freight rate. And, as I understood it, he wanted to know if I saw any reason under that situation for an increase in freight rates, and I said that I thought it was probable, because I could not see otherwise how you could avoid such losses as would be impossible to bear for long.

MR COVERT: Q. Could I put this situation to you: Supposing that the volume of traffic increased to such an extent and the gross revenue resulting therefrom increased so much that it was more than enough to carry the railway over, because the difference between gross revenues and gross operating costs still left them a substantial net profit?

A. That was the actual situation between 1939 and 1943.

Q. Could I just---

A. In a temporary situation of that kind, yes, but all I am concerned---

Q. You think it must be temporary?

A. I think it is nearly inevitably temporary, yes.

Q. Do you not know many utilities in this country that have had increased costs of labour and material, but because they have had increased revenue they have not had to raise their rates for more than thirty years?

A. I know the Bell has gone twenty and is now applying for an increase. I know that Shawinigan has made an increase. I know that the Ontario Hydro has just put in an increase. I would say generally that the more heavily capitalized an industry is, that is, the higher the ratio between its capital investment and its annual sales, the longer it can hold out, but eventually they are all pushed in, and they are all coming in now, even those most heavily capitalized industries.

Q. But I asked you, I think, not if you knew any that had; I asked you if you knew any that had not increased their---

A. I am sorry but I cannot name any who are still on the 1939 rate level.

Q. Have you made a study of it?

A. No.

Q. But you can readily conceive of that possibility, I think?

A. For a time.

Q. Just for a time?

A. For a time, and how long that time will be will depend, as I say, upon the ratio between capital investment and annual sales.

Q. Now, for a minute I want to go to another subject. I wanted to ask you this--if you think it is fair that I should ask you--if you think that the Board of Transport Commissioners should be put in the position of having economic planning powers? If you do not regard it as a fair question --

A. I will pass that. I do not believe so, no.

THE CHAIRMAN: Q. You do not believe they should?

A. I do not believe they should.

MR. COVERT: Q. You think that they should not have broad economic planning powers?

A. I believe it is in a sense a court, that it acts as between the railways on the one hand and the general public upon the other, that it has an obligation to both, and that its primary function ought to be in relation (a) to discrimination and (b) towards control over that element of monopoly power which comes when the earning upon the capital invested in the utility exceeds what may be regarded as the normal competitive return.

THE CHAIRMAN: Q. Do I understand from that, Professor McDougall, that the judicial function of the Board would begin with discrimination, when discrimination is charged and not until then?

A. On discrimination as to excessive earnings.

Q. You see I say that because the present Railway Act says it shall be the duty of the Board to fix just and reasonable rates. You would put that aside?

A. Oh no, I think that remains.

Q. How does it remain?

A. The standard mileage rates - are they not almost in the nature of a hunting license? They do not affect the general flow of traffic.

Q. Then you do not go as far as I thought you were going. You would still have the Board fix ceiling standard rates. It is below that that you would allow the railways latitude to roam. Well, they do today, and my understanding is that discrimination comes in where rates are alleged to be too low in one place and they are unjust to shippers in another place on the same line of railway.

A. I think I must be consistent and I must take your interpretation of what I say, with the railways primary duty being to set rates and the Board strictly as a judicial body deciding whether there was or was not discrimination and that the power to set just and reasonable rates should go.

Q. Then you would change the Act?

A. Yes.

THE CHAIRMAN: If there is to be an amendment to that effect, Mr. Evans, we should have it.

MR. EVANS: No, sir, no amendment.

THE CHAIRMAN: You do not adopt his view.

MR. EVANS: No, sir; he is expressing his own views.

THE CHAIRMAN: All right.

MR. COVERT: Q. I think in fairness to you. Dr. McDougall, you said this would be their primary function but

1. The first part of the report is a general introduction to the project, which includes a brief history of the project and a statement of the objectives.

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they would still continue with other functions, for instance, the safety function, the same as they do now?

A. Broadly, yes; I have not examined this carefully.

Q. But what you are saying . . . as I understand it, is that their main duty--and it is a duty to the railways as well as to the public--because your view, I think, is that the railways are important to the public?

A. Yes.

Q. But they should attempt to enable the railways to earn a fair return on their rate base?

A. Partly because I believe that the public has more to gain by vital railways which are active technically -

Q. I do not want to go into the reason. I think perhaps, Professor McDougall, we could cut it down. I think you have expressed that reason before. I just wanted to say this. You say one of the primary functions of the Board of Transport Commissioners is to see but not to guarantee that the railways at least have the opportunity --

A. Yes.

Q. -- to earn a reasonable return on their rate base. You go further and say that as far as the C.P.R. is concerned they are conservative or modest when they say the return should be somewhere in the nature of 6.5%?

A. May I give my reasons?

Q. Well, I think you have given them.

A. No, I have not.

Q. Then go ahead.

A. What I am saying is this, that when a government, which has the object of setting policy, inflates currency, it is in a very weak moral position when it turns around and tries to hold a public utility to a return upon original cost in dollars of higher value than those which now circulate.

Q. Before you leave that, when you say the government tries to hold them to that I do not quite follow that.

A. If you insist upon the original cost basis, that is, if the Board of Transport Commissioners insists.

Q. Is it the Board that is holding them to it or the government? I do not follow it.

A. Well, it will be an agency of the dominion government, the Board of Transport Commissioners.

Q. An agency of the dominion government.

A. I think so.

THE CHAIRMAN: Q. It is an agency of Parliament.

A. An agency of Parliament.

Q. By the Act.

MR. COVERT: Q. Go ahead.

A. Well, I was merely going to give the changes in the money supply. I will not read them year by year, but in 1938 it was \$1,088,000,000, and in 1949 \$4,422,000,000. The reference is pages 30 and 31 of the Bank of Canada annual report for 1949.

Q. As I say, you did suggest that the C.P.R. was modest or conservative in their suggestion of somewhere in the neighbourhood of 6.5%. You suggested it should be a higher rate of return?

A. Yes.

Q. I wanted to be clear that you think that earnings from rail alone should be sufficient to enable the Canadian Pacific stock to sell at par. Is that your view?

A. Yes. May I explain why?

Q. O.K.

A. What I am saying is this, that so far as regulation is applied it ought to be applied to the property which is devoted to the public service, and if that property is by itself substantially greater than the par value of the

stock then that is the deciding factor, and what the Canadian Pacific does as a corporation outside of the regulated field is no concern of the regulatory body.

Q. Now, you say that it should be higher, as I understand it, because you say the historic cost less depreciation is approximately \$1,001,000,000?

A. Yes.

Q. And that in your view the assets used in railway operation are worth a great deal more than that today?

A. Yes.

Q. And that the proper way to find the return is to value what that is worth today?

A. Yes, that is the counsel of perfection.

THE CHAIRMAN: Q. What?

A. The counsel of perfection. I am willing for the time being to go along with the historic base, the original cost base with an inflated rate of return.

Q. You would?

A. Yes.

Q. The rate to be earned is your way of meeting the situation?

A. Yes.

MR. COVERT: Q. What you would say then is if you could determine what the reproduction cost plus observed depreciation -- I think that was your formula?

A. Reproduction cost of an equivalently useful property.

Q. Less observed depreciation. If you could practicably determine that that would be ideal?

A. Yes.

Q. And then you would apply perhaps to that a 6.5% rate of return?

A. Yes.

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Q. But since the \$1,001,000,000 is lower than that value you say the rate should be higher on that \$1,001,000,000, that is, higher than 6.5%, so in effect what you are trying to do is to give a proper return to the railway on what you say is the correct formula by placing a larger rate of return on what is really a smaller rate base than should be used?

A. Yes.

Q. Now, you had not calculated at all what you thought that rate of return should be on the \$1,001,000,000?

A. No.

Q. Now, tell me this, Dr. McDougall. Do you know of any railroads in the United States whose common stock is selling at par?

A. I think Union Pacific but I cannot guarantee that. I do not follow the American market.

Q. You did not make a study of this at all?

A. No.

Q. But a man of your wide general knowledge would know, I presume, if it were a common thing for railway stocks in the United States to be selling at par?

A. Yes.

Q. You would know that?

A. There are not many, no.

Q. And, as a matter of fact, nowhere near par?

A. For many, yes.

Q. And have not been for a long while?

A. No, not since about 1929.

Q. Do you know if there is any real thought that they will be?

A. Well, do you want to go into a whole discussion of United States policy?

Q. Perhaps that is an unfair question anyway. Now --

Q. But since I am not a member of the

value you say that I am not a member of the

\$1,000,000,000, that is, \$1,000,000,000, as in the

what you are saying to me, that I am not a member of the

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a large sum of money, that I am not a member of the

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Q.

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A. No.

Q. Now, still more, I am not a member of the

that I am not a member of the

well, now, I am not a member of the

Q. I think that I am not a member of the

I am not a member of the

Q. You did not make a study of this at all?

A. I did.

Q. Now, I am not a member of the

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in the United States to be willing to pay

Q.

A. I am not a member of the

Q. I am not a member of the

A. And, I am not a member of the

A. I am not a member of the

Q. And I have not been a member of the

A. No, not since about 1929.

Q. Do you know of any other persons who

with pay

Q. Well, I am not a member of the

that I am not a member of the

Q. I am not a member of the

A. I really would like to do so if you would take it but I am not insisting.

Q. Oh, I do not think it matters much, Professor. Let us pursue it along this line. Then there must be some special reason why the Canadian Pacific should be put in that position in your view?

A. You mean a special position as against United States railroads?

Q. No, put it this way, different than practically any other railway. I think there may be and I am asking you if you think there is because if you do I propose to pursue it further.

A. You see you compel me to open the United States situation. What I am saying is this, that there is in the United States, even more strongly than here, a promotional policy towards other means of transportation. It has had a most destructive effect upon the value of railway capital, yes. We cannot claim --

Q. Could we put it this way, that really the Canadian Pacific is not comparable with United States class one railroads as far as having their stock selling at par?

A. Not in many respects.

Q. Then, as I say, you think there is a sound reason for having Canadian Pacific stock selling at par?

A. Well, so far at least you have had less motor competition and less water competition even than you have in the Mississippi valley. You have not had our Board of Transport Commissioners compelling the railways to make joint rates with barge lines at ^a lower level than the all rail rate. There are a great many reasons. Second, I will say that as a pure matter of economics I think that the promotional policy means a net reduction in the American standard of living rather than an increase, and

it would be worse here.

Q. I will see if I can bring this picture to you. I would suggest to you that whether or not it is important that Canadian Pacific common stock should sell at par really depends on whether or not the Canadian Pacific must continue as a free enterprise?

A. No, I disagree. I believe the important reason is the necessity of additional capital expenditures. If there were no necessity for additional capital expenditures the stock could stay below par for a very long time and there would be no public reason to do anything about it.

Q. Then let me put it this way. Do you not think that if the Canadian Pacific is to stay a private enterprise that it must keep up with the times, it must go into large capital expenditures, for instance, the dieselization programme? Must it not put itself in the position where it can compete with the C.N.R? Must it not be put in the position that it must be able to provide necessary services at the most economical cost to the Canadian producer and manufacturer?

A. But in relation to your dieselization programme it will wash its own face. You do not need to worry about that.

Q. Would you explain why?

A. Yes. It can make more money; it will save enough money so that the savings will pay the cost, I think.

Q. That is my point. We are certainly at cross purposes. Let me put it to you this way. You heard

Mr. Newman. You would agree that it is perhaps highly important that the Canadian Pacific should be enabled to carry out the plan - I think they said it was not a programme - that he suggested?

A. I think it important that this investment be made --

Q. Could you not answer that yes or no? You couldn't, eh?

A. No.

Q. All right, go ahead.

A. I think it important that these investments be made for the service of the traffic. Who makes them --

Q. With respect that is not what I asked you. Would you read the question?

-- Reporter reads:

" You heard Mr. Newman. You would agree that it is perhaps highly important that the Canadian Pacific should be enabled to carry out the plan -- I think they said it was not a programme -- that he suggested?"

MR. COVERT: Q. I will shorten the question. Do you not think it is important that the Canadian Pacific should be in a position to carry out that plan?

A. Yes.

Q. Now, that plan, as he advanced it, will save the country money?

A. Yes, but remember I am not saying it is important to the C.P.R. as a private enterprise; it is important to Canada.

Q. We will come to that.

THE CHAIRMAN: We will have a recess now.

-- Recess.

(Page 17953 follows)

---On resuming:

MR. COVERT: I think Professor McDougall, we do agree that it is important that the Canadian Pacific should be enabled to carry out this plan proposed by Mr. Newman, and then if we have not agreed to it already, perhaps we can agree that in order to do this they must be able to raise substantial sums of money?

A. Yes.

Q. And in order to raise these substantial sums of money it is your view that certainly they must be put in the position of being able to raise certainly a large part of that by the issue and sale of common stock?

A. Yes.

Q. And you go further and say that to do that it must sold at par or above?

A. I say that unreasonable rates are an exploitation of the public; to compel the railway to sell stock at less than the worth that is presently there is an exploitation of the railway, ^{or, I should say,} of the railway shareholders.

Q. But you could not agree with the simple proposition that they must be able to sell it at par or above?

A. Well, if they sell to their own stockholders at par then the exploitation is less, but it is still exploitation if they are not able to hold the value of the stock at somewhere near its book value defined as I defined it.

Q. We cannot get down to the simple proposition that it is necessary to sell it at or above par?

A. Life is rarely simple, Mr. Covert.

Q. Well then your answer to that is "No, we cannot agree to that"?

A. We agree subject to qualification that it is bearable there, it is better above.

Q. Do I gather from that that it is possible to finance by the sale of shares below par but that you say it is unfair to existing shareholders?

A. It is illegal to sell below par, or to attempt to, I should say.

COMMISSIONER INNIS: Q. Could it be made legal?

A. Parliament is omnipotent.

MR. COVERT: Q. But you say that it is unfair to existing shareholders to sell below par?

A. Yes.

Q. So could we say this, that in your view it is essential that the stock should be put in a position that it can be sold at par or above.

A. Yes.

THE CHAIRMAN: Q. How would you find that out, that it could be sold at par or above?

A. The market will tell because the market is where earning power is valued.

Q. You mean the stock market?

A. Yes. Again averaging over a period and not as of one particular day or month.

Q. Does it follow in your view automatically that if you increase freight rates to a certain level/that you must have it in mind Canadian Pacific the stock market will bring/shares up to par.

A. Provided other costs do not absorb what is there done. It is at least conceivable that even though the freight rates increase, other costs would increase so

rapidly that the change in net is either zero or negative. Now, if that occurs you have not produced your result.

MR. COVERT: Well then, Professor McDougall, can we get to this, that in your view if the company is to proceed with a plan such as suggested by Mr. Newman it is highly important to Canada that the regulatory body should enable the company to put in freight rates that will enable the Canadian Pacific to sell its stock at par, if that is possible?

A. Yes. That is on the assumption that the company is reasonably intelligent and efficiently managed.

Q. Yes. And I think you would go with me on this that if there was a reasonable probability that the Board of Transport Commissioners did consent to increases that would enable the Canadian Pacific to secure revenue that would bring about this desirable situation, that that is a desirable end?

A. Yes.

Q. And that if that did occur probably the rate of return required would be less if the investing public were pretty sure that that was going to be a regular thing?

A. Yes.

Q. So that in effect you think they should be put in the position of such utilities as Bell Telephone has been, shall we say, in the past, because the investing public in the case of Bell have been more or less satisfied apparently that Bell was pretty well assured of a steady revenue which would enable them to pay steady dividends?

A. Yes.

Q. And consequently that enables Bell to sell its

shares at perhaps a lower rate of return than Canadian Pacific?

A. Yes.

Q. As a matter of fact the yield on Bell Telephone shares is less than on Canadian Pacific shares today?

A. Very much so, yes.

Q. And probably the reason is that the investing public is more certain that the yield on Bell Telephone will be steadier than the yield on Canadian Pacific?

A. I believe so, yes.

Q. And that the investing public is perhaps worried about the position of the Canadian Pacific,-- they do not know perhaps because of these rate cases that the yield on Canadian Pacific shares will be steady?

A. I believe so, yes.

(Page 17958 follows)

Q. That in your view is a bad situation?

A. I believe so, yes.

Q. Therefore I think perhaps we are in agreement that it is highly desirable that Canadian Pacific common shares should be on the basis that the public would be satisfied that there normally would be a steady return?

A. Do you mean steady from year to year or that upon the average it would be good?

Q. Well, we will say on the long average.

A. Yes, on the long average, certainly.

Q. Now, to put the Canadian Pacific in that position it might take some period of time so that the public would have that confidence?

A. It might, yes.

Q. And would you say this, that if they were on a rate base and rate of return, in your view would that end be achieved more quickly than if they were on a requirements basis?

A. Yes.

Q. Now, if they were put on that basis, Professor McDougall, do you think that the Board of Transport Commissioners should be in the position of being a very capable referee?

A. They ought regardless.

Q. Regardless of whether or not they are on a requirements basis or a rate of return?

A. Yes, sir.

Q. You do not think that it makes any difference?

A. No.

Q. Would you say that it is in your opinion very important that they should be a capable referee?

A. I would think so, yes.

Q. And that they should have a staff fully capable of

studying the affairs of the Canadian Pacific -- I do not mean put them in a position where they would attempt to manage, but they should be able to check very carefully---

A. Oh, yes.

Q. ---for instance maintenance?

A. Yes. May I put a qualification?

Q. Yes.

A. I am thinking only in these terms, that where you are talking about an average return, I doubt the wisdom of any very close argument on any one particular year. I think it ought properly to be on the average, not on the year; but, subject to that, yes.

Q. Now could we go this far, Professor McDougall, that if they were put on a rate basis and rate of return, with an attempt to bring about this desirable situation that they are in a comparable position with other utilities in Canada that have over a long period of years reached the position in the mind of the investor that the return is going to be steady---

A. Yes.

Q. If such were the case, that the Board of Transport Commissioners should reach a position where they were regarded generally as a very capable referee?

A. I would not put the emphasis on the word "regarded". I would have them capable, and let them establish themselves.

Q. Now, would you think, Professor McDougall, that although in the initial stages the rate of return that was required might be quite high, over a long period if this steadiness of payment of dividends to the common shareholders resulted, that rate of return might be lowered?

A. Oh, I believe it would be lowered, yes, but I am speaking now not absolutely but relatively. It is subject to what happens to the general market in interest rates.

Q. You feel, Mr. McDougall, that the Canadian Pacific must be the yardstick for Canadian railways?

A. I do not know of any other position that is possible, since it is the only large privately-owned railway.

Q. And that the Canadian National cannot be the yardstick?

A. No, not under that condition.

Q. It seemed to me that you did lay emphasis on the fact that this is so because it is a free enterprise?

A. Because it must rely solely upon itself, yes.

Q. Would you think that it was being put in a preferred position when it is made the yardstick?

A. No, because so long as Canadian National is not self-sufficient it is in part the beneficiary of these promotional activities which are presently disturbing the whole transportation pattern.

Q. I just missed you there; would you repeat that?

A. Yes; so long as Canadian National is not totally self-sufficient, financing on its own responsibility, paying all its own costs, then it is to that extent being promoted by a government, by social forces, which are at the same time regulating C.P.R. and assessing it to corporate income tax, and it is therefore to that extent disqualified as being a yardstick for anything, and certainly as a proper base on which to establish freight rates for the country.

Q. Professor McDougall, did you make a study at all of the situation with respect to railways in other countries where the governments have taken them over, to see the effect that it had had on either the operation of the railways or on the people generally?

A. Not closely, no. I have been trying as best I can to follow the British situation.

Q. Well, that is perhaps too recent?

A. It is a shade recent; but signs are already appearing of rising rates and difficulties as to costs.

Q. Which you would attribute to government ownership?

A. In part, yes.

THE CHAIRMAN: Q. You say in part?

A. In part.

Q. Well, what does that mean?

A. Well, that the fact that you have government ownership may be due to a very large shall I say resistance to the idea of independent business organizations, a general willingness and liking, a desire for socialism or socialization rather than for independence, and, secondly, I think---

Q. I do not see the relation at all yet; perhaps I will. Go on.

A. Perhaps I could state it this way, sir, that the reasons why Britain took over the railways were not specifically railway reasons; they were a general programme for socialization, and you pulled them in regardless. You may have hoped to get a great many thing; in fact you have got higher rates, you have had administrative difficulties, and you are facing now into a position where the railway unions are growing increasingly restive, so that you may find your costs going quite out of hand.

MR COVERT: The Chairman's question I think was directed to that part of your answer, Professor McDougall, where you said that in part these increased costs could be attributed to the government taking them over.

I think that was your question?

THE CHAIRMAN: That was my question.

MR COVERT: Q. And it did not seem to me that you had dealt with that.

A. Well, it is rather hard to find a good example, but I would regard the experience on Newfoundland Railways as being---

THE CHAIRMAN: Q. The what?

A. The experience on the Newfoundland Railways in the last year as being an instance of what I have in mind -- that one of the things that seems to have happened is a general raising of the wages levels on the Newfoundland Railways to the Canadian average figure, and it means a very extensive increase in the costs of operating in Newfoundland.

MR COVERT: Q. Wouldn't that be simply due to the fact, Professor McDougall, that it would be a peculiar situation to have the rates of wages in one province different from the rates of wages in another on the same railway, when in all the other nine provinces they were the same?

A. But if they were not the same railway, then what?

Q. Well, supposing I put it to you this way: Supposing the Canadian Pacific had taken it over---

THE CHAIRMAN: Perhaps Professor McDougall has in mind the condition just before Newfoundland came into Confederation.

THE WITNESS: Yes. If that had been a private railway before Confederation, then there would have been a much greater power to resist increases in wages in order to keep costs and revenues closely together.

THE CHAIRMAN: Q. Does that appear to be the case in Canada? You have a private railway; wages have gone up, have they not?

A. They have, but I do not think that it has been a rise which is totally out of line with the rest of urban employment. I reserve---

Q. You think the rise in Newfoundland was of such a nature?

A. Yes.

MR COVERT: Q. I put this to you: Do you think, Professor McDougall, if the Canadian Pacific had taken over the Newfoundland Railways they would have been able to have a different wage rate in Newfoundland than they would have in their other provinces?

A. I would question, but I would also question the assumption.

Q. That they take it over?

A. Yes.

Q. You would not agree with this, that the very fact that Newfoundland was brought in as another province, regardless of who had taken over the railway -- that that would have meant practically automatically that the rates would have increased so that they would be the same as in all other parts of Canada?

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A. It is very probable, yes.

Q. I still thought that that was not an answer to the Chairman. Perhaps you have not made a study of the situation in Germany or France?

A. No.

THE CHAIRMAN: Q. This may be the time, Mr. Covert. Professor McDougall, I think you were the first witness who threw any light on this question of Government ownership of the entire railway system.

And as I told you yesterday, Saskatchewan had something to say about it in their Brief; and in addition Prince Edward Island makes it a very important and serious part of their case. By the way, have you read it?

A. Yes, sir.

Q. Well then, since you yourself began to talk on the subject yesterday, and since you expressed yourself as being opposed to government ownership, I wondered if you had rigid economic reasons for this opposition?

The a priori reasons we all know. They are argued all the time: that government indulging in business is a bad thing because of political pressure and all sorts of things.

I suppose economic views are gathered by experience. That is why I asked you if you were familiar with the German situation.

A. Not closely, no, sir.

Q. Well, I myself looked up the question, and I found that all the railways in Prussia were nationalized in 1879. That was a long time ago.

A. Oh, yes.

Q. And that after Prussia, the other German states all nationalized their lines in succeeding years; so that

by 1914 practically all the railway lines in Germany were state railways.

Then, after the war, the central government which came into power then, took over all the railways as, you might say, an imperial enterprise, and they have been going on that way ever since.

Surely, there was a subject of inquiry where economists might tell us today what was the result in Germany, what has been the result of state monopoly of railway transportation.

A. I think your difficulty is to relate the German railways to the German economies. If you have a compact country - -

Q. I would have hoped that economists might have made that an important part of their studies. That is how economic laws are evolved, by experience; they are empirical; and I was hoping, when you began your comments on the theory yesterday, that you might be able to tell us what has been the experience, from the point of view of economists, of this very long period of government ownership of all the railways in Germany.

A. I am afraid I cannot.

Q. As I say, the Prince Edward Island Brief is very lengthy; and you have read it, and have read all they say?

A. Yes.

Q. And I take it you disagree with what they say?

A. Yes.

Q. All right. We have it before us. Perhaps, in time to come, Mr. Campbell will be able to deal with it.

MR. COVERT: Mr. Campbell is here now, Mr. Chairman.

THE CHAIRMAN: Oh, Mr. Campbell is here now?

MR. COVERT: Yes, and I understand Mr. Campbell proposes to argue that part of the Brief.

THE CHAIRMAN: Well, Mr. Campbell, I believe you were not here this morning when the question was first raised, and when the provinces were given an opportunity to examine Professor McDougall. Would you like to examine him?

MR. CAMPBELL: I do not propose to do so, my lord, and for the very reason which your lordship has just mentioned to the witness, namely, his disagreement with our position in very general terms.

THE CHAIRMAN: I see. Very well.

MR. COVERT: Q. Now, Professor McDougall, I would like to deal briefly with the question of horizontal increases. My understanding is, that it is the only proper method of applying increased rates?

A. In a general inflation, yes.

Q. Yes, in a general inflation. And would you say that if, instead of the 40% increase which is now in effect suppose the application had been for 80%, would you say that was still the proper method, under the inflationary conditions which you say exist today?

A. Oh, I could not say that. What I do say is this: that the railways applied for an increase too late; and that increase was handled with an extreme deliberation.

It would be much better if they had four twenties rather than one eighty, much better; because, no matter what the increase was going to be, to some extent it would be a new factor which would have to be taken into account; and it is easier to take a small thing into account than to take one eighty per cent jump.

Q. Yes; but, for instance, a 21 per cent jump when it was given; and then a later one of 8 per cent on top of that; and then a 16 per cent in substitution for the 8; you think that the proper method for those cases was the horizontal method?

A. The percentage increase?

Q. Yes?

A. Yes !

Q. And I think you have probably examined the situation in the United States ?

A. Yes.

Q. And you are aware that they have paid considerable attention to the limitations of horizontal increases?

A. Yes.

Q. And you do not think that that is necessary in Canada?

A. No, just because we have national railways, as a major reason.

Q. Because we have national railways?

A. Yes, and that you have no individual railways covering the whole nation. In the United States, even their transcontinentals are Chicago and West.

Q. And that is the reason?

A. It is a major reason, Yes.

Q. It is a major reason; and are there other reasons?

A. Not of any really serious importance, no.

Q. Then, that is really the reason?

A. Yes.

Q. You would not then, I take it, probably disagree with the practice in the United States under the circumstances which exist there?

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A. It is a different economy, yes. I would not disagree.

Q. You would not disagree, but you think that under the situation that exists in Canada, with the two trans-continental railways, that that situation is not a - -

A. That the major reason was washed out.

Q. Yes. Perhaps I did not understand you correctly, but I want to get on common ground with you. I understand that you say that since other costs have gone up to such an extent that the position of the people in, what we call, the extremities of Canada, that is to say, as distinct from the central provinces - -

A. Yes.

Q.that horizontal increases really do not affect them to any serious extent?

A. What I am saying is, that if the transportation cost, as a percentage of the total cost, is not higher now than it was in 1939, then they have not been hurt. But if it is lower, then they have probably been benefitted.

Q. So that freight rates, generally, were the same until from about 1922 to 1946?

A. Yes, that is, the class rates.

Q. Yes; and then, we will say, in 1940 the cost, the other costs: began to rise?

A. You are speaking of total costs or unit costs?

Q. Total costs of production, we will say. Let us deal with the case of a manufacturer in the extremity, in one of the extremities, as compared with the central provinces. Can we deal with it on that basis?

A. You are talking now of a manufacturer, not of the railways?

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Q. That is right.

A. Oh, continue.

Q. That since in 1940 these other costs began to rise, nevertheless the freight rates remained the same.

A. Yes.

Q. Therefore the position of the man in the extremity has really improved?

A. Yes, because his selling prices were increasing yet he had constant dollar transportation costs.

Q. Yes; and in most cases his business expanded?

A. Yes, although I cannot say whether it expanded more, proportionately, than the expansion elsewhere.

Q. Yes. But in any event he was better off as a result of the holding of the freight rates down?

A. Yes.

Q. And he enjoyed that position from 1940 to --?

A. To 1948, April, 1948.

Q. Practically, yes. Now, what you say, I believe, Professor McDougall, is: that if the increase in freight rates by the horizontal method has affected him, perhaps, somewhat in dollars, nevertheless he is in a better position than he was in 1940 still?

A. I believe so, speaking generally.

Q. Yes.

A. And subject, always, to this danger: that he may have put himself out into lines of production where he was encouraged by this thing; or he may have allowed some of his other costs to rise, just because his transportation costs were being reduced.

Q. Yes, but as long as the increased freight rates, by this horizontal method, did not affect him or put him in a position where he was not worse off than he was before

the war, then, perhaps, it is a desirable situation, from your view, to put him back to the position where he was before the war?

A. Only if it is necessary to maintain a prosperous and successful railway, and only to that extent.

Q. But supposing you had a situation where his freight rates in 1940 were higher than perhaps they should have been, as compared with the man in the central provinces?

A. How do you determine what should have been?

Q. Supposing they were built up on a basis that they were 50 per cent higher because of the lack of traffic density?

A. You mean a 50 per cent higher rate for an equivalent mileage?

Q. Yes.

A. That is not a very realistic assumption, is it?

Q. I do not know, Professor McDougall; but may I take that assumption?

A. Yes, we will pass it.

Q. It may be that it was not 50 per cent. It may not have been anything like that. I simply put that as an example. But if, over the years, they did not change, and you start adding horizontal increases to it, as compared with a horizontal increase in the case of the central provinces, then that would accentuate a wrong, if it were a wrong. It would accentuate it further, would it not?

A. If the rates were wrong in the beginning, they would still be wrong; still be wrong proportionately after the change was made, yes.

Q. Yes. And if there were disparities existing prior to the horizontal increase, then those disparities would be increased?

A. Would you define disparities?

Q. Of the nature I mentioned, although it might not be 50 per cent.

A. Yes.

Q. So could we agree on this: that if your assumption that a horizontal increase is the soundest method depends on whether or not the rates were sound in themselves in the first instance, if they are, would there be any disparity?

A. If the rates were ^{not} sound in the first instance, they would be corrected; and having corrected them, then the percentage increase uniformly applied is the correct solution, having regard to the fact that you may be dealing with inflation.

Q. If you are going to apply horizontal increases, then the rates to which they are applied - there certainly should not have been any disparity existing at that time, at the time of the application of the percentage increase.

A. I would rather say: that if you have an inflation, it is a very uncomfortable situation to begin with; and that wiping-up afterwards is a long, arduous, and difficult job. But we live in an imperfect world.

THE CHAIRMAN: Oh, I had no suspicion of that.

MR. COVERT: Q. You would rather give that answer?

A. Yes.

Q. You think we could not simplify it as I have tried to?

A. I believe not.

Q. Very well. Now, on the question of the incidence of freight rates, I would like to ask you a few questions.

I think the Canadian Pacific's position, and your position is, that regardless of who pays the freight bill in the long run, it is, in a very real sense, these freight rates, they are borne by the consumer?

A. Yes.

Q. And you would lay considerable emphasis on the words "in the long run"?

A. Yes.

Q. I think, when you start out with that part of the sentence which says that regardless of who pays the freight bill, you are, perhaps, drawing a distinction between the payment and the bearer?

A. Yes.

Q. And anyone of several persons may actually pay the bill ; but there is a great distinction between who pays it and who bears it. There might well be?

A. Quite!

Q. Now, you also recognize that the incidence is shifted from time to time.

A. Yes.

Q. Now, I would like you to assume with me, for a moment, the case where the freight charges had been unchanged for a long time, and that the price system has adjusted itself to those charges. Now, that would be the case where you would say that in the long run the freight charge is actually borne by the consumer?

A. Yes, and I would add one further assumption: that the general wholesale price index has also been reasonably stable.

THE CHAIRMAN: What is that?

A. That the general wholesale price index has been reasonably stable, as one additional assumption to those which Mr. Covert made.

MR. COVERT: Q. Yes. Now then, I would like you to consider for a moment the question of the increase in freight rates arising after that condition to which I previously referred existed. You would agree that the short-run affect, in such a case, might be quite different from the long-run affect?

A. Yes. Your short-run effect would depend on the elasticity of supply and the elasticity of demand.

Q. There would be quite a few things which would enter into that picture. I suggest to you, for example, the question of whether it is a buyers' or a sellers' market.

A. Yes.

Q. And whether the area is a deficient area or a surplus area?

A. Oh, yes, a lot of things of that kind.

Q. Yes; supply and demand; elasticity and inelasticity, and so on.

I was wondering if we could not get a better word for elasticity and for inelasticity. I find them confusing. Could we say for elasticity - could we call it changeable?

A. You are tampering with a piece of terminology which has a very long history.

Q. You will remember, Professor McDougall, that Dr. Locklin got highly confused with it.

A. Might I try where he stumbled?

Q. Have you got a better word?

A. No.

Q. My difficulty is that every time I use those words elastic and inelastic I get confused.

THE CHAIRMAN: Q. Perhaps we had better have them defined now.

A. It is a case of more or less.

Now, unit elasticity is neither elastic or inelastic. That is the case in which there is a change in volume and there is a proportionate change in price; so that, regardless of the change in volume, the total amount of money paid remains unchanged.

Q. That is very rigid?

A. That is unit elasticity.

Q. It does not waver to one side or the other?

A. In the total money paid. For example, if you sell half as much, you sell it for twice the price.

Now then, an elastic demand is one where, with an increasing volume, you get a larger amount of money paid for the product.

Q. The price increases with the volume?

A. No. But the prices fail to fall as fast as the volume increases.

Q. Fail to fall?

A. Yes.

Q. It ought to fall as fast as the volume increases in order to remain unified?

A. Yes, by unit elasticity.

Q. Yes; and if it does not fall as fast as the volume increases?

A. Then a great many products have increasing volume. They are known as elastic products.

Q. When does it become inelastic?

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A. An inelastic demand is one where, with an increase in supply, the price falls so rapidly that . . . less money is paid for it; or, if the supply falls, the price rises so rapidly that more money is paid for it.

Q. In both those cases it is inelastic?

A. Yes, because of the increase.

Q. I am sorry:

COMMISSIONER INNIS: I think we could simplify this thing a great deal if we were simply to use the words which you suggested, Mr. Covert: changeable and rigid.

THE CHAIRMAN: Q. We have three terms now instead of two. The middle one is unified. On one side of it there is elastic, and on the other side of it there is inelastic.

A. I was only trying to be helpful, I am sorry.

MR. EVANS: Might I offer this: that both Mr. Covert and, perhaps, Dr. Innis, would tend to over-simplify and that perhaps the result might not be too helpful for this reason: that changes are not the test of elasticity in themselves. You must carry with it some result from the changes. You just cannot say that changing demands constitute elasticity.

THE WITNESS: Oh, no.

COMMISSIONER INNIS: I hope we do not become quite so involved.

MR. EVANS: I was hoping for that too, sir.

THE CHAIRMAN: Q. May we not proceed on some basis or other?

A. I shall follow you as best I can, but I may stumble.

MR. COVERT: Q. I just want to get this straight,

Professor McDougall, that, if I refer to an inelastic demand, I could not call it a sort of steady demand; it just does not stretch?

A. Yes, that is partly so; that is, with changes in volume, the demand for a given quantity changed very little; and therefore the price changed very much.

THE CHAIRMAN: Q. Now, is that elastic or inelastic?

A. That, sir, is inelastic.

MR. COVERT: Q. If I referred to an elastic demand, I could not call that a changeable demand. I do not know why I always get so confused, but I certainly do, every time I try. So I wondered if I couldn't get down to a basis?

A. If you would say: a stable demand for commodities, and a changeable demand for commodities, it might make your idea completely clear.

Q. Perhaps I had better abandon this altogether.

THE CHAIRMAN: Yes. We reduced stable to changeable, and now we have two others. We have not got the third. However, it might be better to try to work out some simplification.

We shall adjourn now to this afternoon.

---At 1.00 p.m. the Commission adjourned until 2.45 p.m. today.

OTTAWA, ONTARIO
MARCH 14, 1950.

A F T E R N O O N S E S S I O N

PROFESSOR J. L. McDOUGALL - Recalled

EXAMINATION BY MR. COVERT - (Cont.)

MR. COVERT: I think your lordship will be glad to hear that I have abandoned the question of elasticity and inelasticity.

THE CHAIRMAN: Yes, and I am sure that Professor McDougall will be glad to hear it too.

MR. COVERT: Q. Could we agree that, in general, the existence of transfer costs tends to encourage self-sufficiency of an area by protecting local industry from competition from outside; and that, conversely, an increase in transfer costs would tend to reduce outside competition, and to that extent stimulate local industry?

A. By transfer costs you are thinking, specifically, of transportation charges to move products in and out?

Q. That is right.

A. Yes, I agree.

Q. And would you also agree that where, in a country such as Canada, different regions, to some extent, face competition from other sources of supply, that some regions are more affected than others, and that the effect of increases in freight charges on the products raised in such regions would differ in the manner in which the increase is applied?

A. Are you thinking of an internal market or an external market?

Q. I thought it might apply to both. Do you think there should be a differentiation?

A. Oh!

1. The first part of the document is a letter from the President of the United States to the Congress, dated January 3, 1862. The letter is signed by Abraham Lincoln and is addressed to the Senate and House of Representatives. The letter discusses the state of the Union and the progress of the war against the Confederacy. It also mentions the Emancipation Proclamation and the importance of the Union's victory.

2. The second part of the document is a report from the Secretary of the War Department, dated January 10, 1862. The report is signed by Edwin M. Stanton and is addressed to the President. The report discusses the military situation in the South and the progress of the Union's army. It also mentions the importance of the Union's victory and the need for more resources.

3. The third part of the document is a report from the Secretary of the Navy Department, dated January 15, 1862. The report is signed by Gideon Welles and is addressed to the President. The report discusses the naval situation in the South and the progress of the Union's fleet. It also mentions the importance of the Union's victory and the need for more resources.

4. The fourth part of the document is a report from the Secretary of the Treasury Department, dated January 20, 1862. The report is signed by Salmon P. Chase and is addressed to the President. The report discusses the financial situation of the Union and the progress of the war. It also mentions the importance of the Union's victory and the need for more resources.

5. The fifth part of the document is a report from the Secretary of the Interior Department, dated January 25, 1862. The report is signed by Caleb B. Smith and is addressed to the President. The report discusses the land situation in the South and the progress of the Union's army. It also mentions the importance of the Union's victory and the need for more resources.

6. The sixth part of the document is a report from the Secretary of the War Department, dated February 1, 1862. The report is signed by Edwin M. Stanton and is addressed to the President. The report discusses the military situation in the South and the progress of the Union's army. It also mentions the importance of the Union's victory and the need for more resources.

7. The seventh part of the document is a report from the Secretary of the Navy Department, dated February 5, 1862. The report is signed by Gideon Welles and is addressed to the President. The report discusses the naval situation in the South and the progress of the Union's fleet. It also mentions the importance of the Union's victory and the need for more resources.

8. The eighth part of the document is a report from the Secretary of the Treasury Department, dated February 10, 1862. The report is signed by Salmon P. Chase and is addressed to the President. The report discusses the financial situation of the Union and the progress of the war. It also mentions the importance of the Union's victory and the need for more resources.

9. The ninth part of the document is a report from the Secretary of the Interior Department, dated February 15, 1862. The report is signed by Caleb B. Smith and is addressed to the President. The report discusses the land situation in the South and the progress of the Union's army. It also mentions the importance of the Union's victory and the need for more resources.

10. The tenth part of the document is a report from the Secretary of the War Department, dated February 20, 1862. The report is signed by Edwin M. Stanton and is addressed to the President. The report discusses the military situation in the South and the progress of the Union's army. It also mentions the importance of the Union's victory and the need for more resources.

Q. Let us take internal markets.

A. On an internal market, if you have an increase in transport costs in step with other prices, then I think there is no difference. But there will be a difference in relative advantage.

THE CHAIRMAN: Q. In relative advantage?

A. Yes, in relative advantage, if some other method is used of increasing the freight charges.

MR. COVERT: Q. The whole point, you say, depends on whether or not the increases are in step with other prices and other costs?

A. Yes.

Q. Would you agree with this proposition: that increases on a horizontal method offer the transfer cost relations between long and short-haul?

A. Is that sentence completed?

Q. Yes.

A. Well, if there was a balance before, the same balance remains afterwards. That is, if you will turn - is it page 57?

Q. You mean those examples?

A. Yes.

Q. Then again, you say that depends on whether there was a balance before?

A. Yes.

COMMISSIONER ANGUS: Q. You mean before the period during which prices have been rising?

A. Prices and railway rates have been rising, yes.

Q. But not just before the increase in rates?

A. Oh, no.

MR. COVERT: Q. Would you say, Professor McDougall, that, dollar-wise, the man in the extremity, using that word as we were using it this morning, is worse off as a result of horizontal increases?

A. He is getting more dollars and he is paying more dollars, so he is neither better nor worse off.

Q. Than he was immediately before the increase?

A. Before the general increase in prices.

Q. Before the general increase in prices.

I wonder, Professor McDougall, if you have examined Professor Locklin's book "Economics of Transportation"; I mean the 1949 edition, at page 40?

A. I have the third edition here, which is 1947. Probably the one you have is just a second printing.

Q. Perhaps it is. You might turn to page 40 and see. It seems to me that he felt that percentage increases in the United States in 1918 and 1920 had worked great hardships on manufacturers, dealers, and farmers who had long hauls. Do you recall that?

A. Whereabouts on the page is that?

Q. It may be on a different page. Yes, he says here:-

"There is plenty of evidence that the freight rate increases of 1918 and 1920, which were percentage increases, had this effect: working hardships on manufacturers, dealers, and farmers who had long hauls."

A. But did they have that effect at the time when the rates were increased and prices were rising, or did it have that effect, after the boom had broken and prices had fallen?

Q. Take 1918. Perhaps you could tell better than I can.

A. I do not think it did.

Q. And the same in 1920?

A. Once you come past, say, September 1920, then you have a position in which railway rates were one of the items which did not come down as much as other prices. Then you may have had difficulty. But I do not see that you had it at the time when both rates and general wholesale prices were rising.

Q. Then it is your view that that is the whole test of the matter and it lies in that one point: were other prices rising at the same time?

A. I think that is the cardinal point, yes.

Q. And if the position is such that freight rates, once they are raised, tend to stay at that level, and prices may go down, then, would you agree that in circumstances of that kind, there may be hardships on manufacturers, dealers, and farmers who did have long hauls?

A. Well, if I may split that and treat first with the farm position, which is, I think, for Canada the most important, that if you were to get - and I am making an assumption which I think is not realistic, but I think it is at least open to be contemplated - if you were to get a situation of a drastic fall in prices of farm products, that is, export farm products, whereas the protected sector of the economy, not only the railways, but internal services, the manufactured goods tended to hold up in prices, then, obviously, there is a very sharp transfer of social income away from the farmers towards the protected people.

But your difficulty there is not a difficulty of freight

Q. Now, I suppose you could tell better than I

can.

A. It is not certain at all.

Q. At the time the body

was found, was it in the same position as

it was when it was first found? Was it in the same

position as it was when it was first found?

Q. You have seen the body, but you do not know that

it was in the same position as it was when it was first

found, is that right?

A. I am not sure, but I think it was in the same

position as it was when it was first found, is that

right? I am not sure.

Q. I think it is the same position as it was

when it was first found, is that right? I am not

sure, but I think it was in the same position as it

was when it was first found, is that right? I am

not sure, but I think it was in the same position as

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it was when it was first found, is that right? I

am not sure, but I think it was in the same position

as it was when it was first found, is that right?

Q. I think it is the same position as it was

when it was first found, is that right? I am not

sure, but I think it was in the same position as it

rates as such. It is a difficulty of having two sectors of the economy moving in opposite directions.

I am saying that the railway rates and costs should, in such a situation, be brought down so that the two can come again into harmony. But do not rivet your attention on the railway rates and leave all the rest of the protected sector out of your attention. It is a general economic problem. It is not a railway problem.

Q. That is one part of the split. What is the other part?

A. Well, I am hard put to it to see how he would justify it in relation to the manufacturer and dealers, the dealers especially, since the dealers are going to be able to adjust themselves quite rapidly. The problem of the farmer is analagous to the problem of the railroad, because his capital investment is high per dollar of annual output.

Q. And the manufacturer?

A. The manufacturer falls into the intermediate position, and I would question whether his troubles were severe.

THE CHAIRMAN: Q. Whether what?

A. Whether his troubles were severe. He could adjust himself within a reasonable time, perhaps, let us say, a year. There may be a problem of transition, but he will make the change fairly rapidly.

MR. COVERT: Q. But then, as I say, coming back to my question, if it were so, that once the rates were raised and they tended to stay at that level, I take it you could not agree that it would work any greater hardship on the manufacturer, the dealer or the farmer who had a long haul than it would in the case of the same classes who had a short haul?

(Page 17989 follows)

A. I would strongly question it. I think there might be cases where that would occur but I think they would tend to be special cases.

Q. Now then, in the case of a deficit area which might rely on outside sources for capital and consumer goods, for example, the prairie provinces with respect to farm implements, would you agree that in cases of this kind increases in freight charges tend to be passed on to the consumer in the deficit area?

A. I think I said that freight, as one of the costs of production, is always passed on, unless there be some special disturbing circumstances.

Q. And the further away the farmer is from the source of supply the more he must pay?

A. It will depend entirely on the manufacturing margin and the position of the dealer, that if the dealer wants to absorb he will absorb. The nearest approach I can give you is the matter of marketing motor cars under the conditions, say, of 1939. The gross margin was in substantial part absorbed by the dealer in the trade-in price on the old car, and if the competition between dealers is sharp enough then part of that margin will be absorbed in that fashion. If there is no competition, or if people ^{more} are anxious to get the cars ^{than they are to get them} at low prices, dealers' margin will very rapidly absorb a great deal more than the transport cost.

Q. Take the case of the sale of a car in times when there is a large demand for cars, then the person who is farthest away, of course, pays more for the car because the freight charges are added to it.

A. He may also pay more for the car because the dealer's margin is wider there than some place else,

I could not say.

Q. But you would not agree with the first proposition?

A. I would say there is a probability, not a certainty.

Q. And if the horizontal method ^{of} increase ^{is} applied in that case wouldn't he be affected to a much greater extent than otherwise?

A. Well, your increase in car prices has been very close to the one hundred per cent. If he is paying the same percentage in transport costs or less, -- I think I have transport costs on motor cars for quite a number of destinations if you will let me look them up.

Q. Go ahead.

However, you suggested his position is relatively not different?

A. I would think probably not, no.

Q. And it is the same, as I say, with the farmer in respect to farm implements?

A. Yes but I think if you are going to understand what happens to retail prices you are likely to get a good deal further if you keep an eye on the dealers' margins than if you fix your eyes on the freight alone.

Q. In the case of things like farm implements?

A. Even in farm implements or automobiles or, as I said this morning, cement, which to me was a most surprising case.

Q. Why do you say cement is surprising?

A. Because it is so heavy and it is relatively low in value per pound.

COMMISSIONER INNIS: Q. Did you go into a study of their price fixing policy at all?

A. This was strictly a study of what prices were at the retail level. Now you had dealers' margins,

if I can quote from memory, which ran between 19.5 per cent and 45 to 50 per cent, -- of course, there were quantity discounts around there but we ^{will} neglect them. Now, whether the margin was 20 per cent or 50 per cent depended upon how sharp the competition was between the dealers in building supplies.

THE CHAIRMAN: The dealers in what?

A. In building supplies.

If there were three of them and the competition was sharp you might get 20 per cent; if there was one you might work closer to 50 per cent.

Q.
COMMISSIONER INNIS: The same brand of cement?

A. The same cement. Cement is a standardized product; no matter whose you buy you ^{still} buy Portland cement at a given grade.

MR. COVERT: Q. And, Professor McDougall, would you disagree that the impact ^{of} increases in freight charges would be more serious on producers in areas that are more specialized economically than on ^{producers in} areas that are more widely diversified?

A. Again I am forced back to ask what is the general market situation. I think it is not a matter ^{solely} of specialization as it is a lack of alternative opportunity. If you have an area which can produce one thing and one only and the market for that particular product goes bad then those people are in a bad position, no doubt about it, and I do not believe that any freight rate change can make much of a difference to them. I wonder if you noticed in the press inside the last ten days the suggestion that by next September there may be an egg shortage? Now, that means that there has been a complete realignment of the poultry industry inside less than twelve months, that is,

that people who were producing eggs have been able to make the appropriate adjustments ^{to price ;} /they have gone to do something else, and you again bring the price of eggs back to what they think is a normal price giving them a reasonable return.

Q. I noticed you used the word 'solely'. I just wonder if you would agree that there was a difference between the case of a producer in the area which is specialized economically as compared with one in an area where there is diversification of production. Do you think there is any difference at all, Professor McDougall?

A. It is not so much that they are specialized, it is that they lack alternative opportunities.

Q. Put it either way you like but do you think there is any difference in the impact of freight rates in such a case?

A. Yes.

Q. You do.

A. I am not certain that I am being quite clear with you. What I am saying is that a man might be highly specialized just because the price situation is favourable; but he has an easy out, he can move to something else quickly, in that case he is going to be all right.

Q. You mean in an area where there is a diversification?

A. In an area where there is potential diversification, it need not be actual. Then if there is a ^{potential} /shift that pays better the shift will take place quickly. If there is no alternative, then it may be tough.

Q. Would you think that the effect might be different in the case of an area which is expanding in an economic sense as compared with the effect in an area which is static? For instance, you might take Mr. Frawley's province, Alberta, as an example of the one, and Prince Edward Island as an example of the other.

A. There would be a difference. I think you would have to examine each individual case to see how much or for how long it would remain.

Q. I think perhaps we had agreed that in a seller's market the freight increases tend to be passed on to the buyer immediately?

A. Yes.

Q. And that in a buyer's market they tend to fall on the seller?

A. Yes; that the consumer gets the advantage in the buyer's market, yes.

Q. Will you agree that in the case of industries such as agriculture, where over long periods of time the supply is quite fixed, adjustment as far as freight rates are concerned takes a much longer time than in cases where this is not so?

A. I do not think it is safe to say that in agriculture the supply is fixed, because obviously it varies very sharply as between years.

Q. I said over a long period; perhaps you cannot even make that assumption, then?

A. Well, I was only going to say that in agriculture you tend to get a relatively constant input of effort but a fairly wide variation in output due to climatic factors; that the output of agricultural products is primarily a function of climate and only secondarily a function of the effort put in.

Q. Would you repeat that, please?

A. I say that the output of agricultural products is primarily a function of the climate and only secondarily of the amount of effort put in by farmers to production. Now, that is most clear in the prairie provinces, but it is a general statement.

Q. Incidentally, Professor McDougall, this morning we were discussing this 4.5 figure; you said that that was weighted?

A. Yes.

Q. How did you get that? How was that figure arrived at?

A. It is the gross revenue freight and gross revenue switching from the Statistics of Steam Railways applied against the gross national product from the Canadian Statistical Review.

Q. In other words, you just find the percentage that the total freight paid to the railways -- freight and switching, you said?

A. Yes.

Q. Bears to the total---

A. Of gross national product.

Q. ---of gross national product. And you say that gives you a weighted average?

A. Yes.

Q. Would you agree with this statement, that in a surplus area the price is roughly equivalent to the primary market price less the cost of marketing? Will you go that far?

A. That is, when a general market price has been established?

Q. Yes.

A. The value let us say at the farm will vary with

the distance from the central market? Yes.

Q. The way you put it, does that mean the same as the way I put it?

A. I think so.

Q. Then could you just agree with the way I have put it?

A. Well, I wanted to make quite certain that we had a general market. If you have not got a market at one particular point, then you leave me in a difficulty; I would have had to make a longer answer.

Q. Let us assume the general market, then, and I say that in a surplus area the price is roughly equivalent to the primary market price less the cost of marketing?

A. Yes.

Q. In a deficit area, that the price is roughly equivalent to the price in the farthest producing area from which it draws its supply, plus the cost of transportation?

A. I think you would be safer if you said that it was the cost at the central market plus the cost of moving from the central market to the point of demand.

Q. I think that is the same, isn't it?

A. Well, I think it is clearer my way.

Q. Well, is there any doubt about it my way?

A. Yes, because you are taking a referred price in the one case.

Q. Just a minute, now. Equivalent to the price in the farthest producing area from which it draws its supply, plus the cost of transportation; and I have prefaced it by, roughly equivalent to that price?

A. Well, I do not want to split hairs, but the difficulty is that you are really using a marginal concept, and the marginal supply need not come from the farthest point.

...to that
A. Well, I do not want to say that, but the difficulty is that you are really using a marginal concept, and the marginal supply need not come from the farthest point. A. I think you would be safer if you said that it was the cost at the central market plus the cost of moving from the central market to the point of demand.

Q. I think that is the same, isn't it?
A. Well, I think it is clearer my way.
Q. Well, is there any doubt about it my way?

A. Yes, because you are taking a referred price in the one case.

Q. Just a minute, now. Equivalent to the price in the farthest producing area from which it draws its supply, plus the cost of transportation; and I have prefaced it by, "A. Well, I do not want to say that, but the difficulty is that you are really using a marginal concept," and the marginal supply need not come from the farthest point. I think you would be safer if you said that

from the central market to the point of demand.
Q. I think that is the same, isn't it?
A. Well, I think it is clearer my way.

Q. Is there any doubt about it my way?
A. Yes, because you are taking a referred price in

Q. Just a minute, now. Equivalent to the price in the farthest producing area from which it draws its supply, plus the cost of transportation; and I have prefaced it by,

I am trying to be helpful.

Q. Very well. Now, could we say, then, that in either case the most distant producer will receive the lowest price at the farm or factory?

A. That would be the tendency, yes -- that is, if that is in an export area, and then only.

Q. That only applies, you say, in the case of an export area?

A. Oh, yes. A good deal of the settlement of the Ottawa Valley here was built upon a specialized market in hay and oats for the service of lumber camps, where you got a very much higher price than the central market price; you got the central market price plus inbound transport.

Q. There was one point on which I touched this morning, Professor McDougall; I just wanted to take it a little further. You would agree that during the war other costs had increased and freight rates remained fixed, and I think you agreed that this would result in some measure of benefit to the extremities?

A. Yes.

Q. And that this might cause the industries in the extremities to expand?

A. It might cause them to do many things. They might expand, they might bid up the prices of the factors they were using. All those things are possible, yes.

Q. And if they were on what perhaps might be called a marginal basis before, this might raise them up above that basis so that they could perhaps go further, extend their territory of sales to a larger extent?

A. Yes, it would have that tendency.

Q. Then in that case would you agree that the horizontal increase in freight rates might tend to put them back in that marginal position that they were in before?

A. It would tend to reduce the area over which they could market, yes, but the moving factor, the cause of present loss, is the fact that the rates were not increased as early as they should have been.

Q. Now, there are a few points in your evidence of yesterday that I would like to discuss with you.

COMMISSIONER INNIS: Before you start, Mr. Covert:

Q. The interest you show in this matter of the shift would seem to lead one to infer that you favour an economy that is manoeuvrable and easily shifted, shifting from one commodity to another in the face of strains?

A. In so far as it is possible, it is certainly better to be flexible than to be inflexible, yes.

Q. But you do not take into account the cost of shifting? After all, in most cases there is considerable economic loss involved in moving from one commodity to another.

A. Oh, yes, it is difficult, but if markets change what do you do? I am not putting it forward as being inherently good that markets should change; I am merely saying that since you have to take into account that markets do in fact change, you had better be quick on your feet if you can.

Q. I was just wondering whether there was some danger of more or less compelling the Canadian exporter or Canadians generally to be the sort of person who hops around from one thing to another?

A. If you think of the exporter solely, I think I put it very clearly, that I figure that where export conditions change the burden ought to be very much more widely dispersed than it ever has been before in this country. What we have done I admit is to try and concentrate the burden first upon the exporter and then when the

effect seeps out from him to take it in terms of unemployment in the rest of the community rather than terms of prices that are consonant with the current prices of our exports. Now, that is deplorable; I think it is deplorable economically; I think it is also largely stupid, but I think it is a description of what we have done.

Q. I was thinking of the case of poultry which you mentioned; it would not be fair to say that you got a good deal of pleasure out of seeing the man shift from one thing to another, but I do not think you expressed much sympathy for him.

A. Well, I am saying only that they went through a very difficult position, and have done it with an extreme speed, yes. Now, if you say do I enjoy seeing people lose the capital they have invested in henhouses and such like, no, I do not, but what do you to guarantee a market for eggs to people who cannot pay for them?

Q. I am thinking of the sort of economy that you have in mind, whether it is one that is highly manoeuvrable, capable of rapid shifts, or one which is reasonably stable, one upon which you can depend to a considerable extent for continuity and so on?

A. Well, if the choice were open to Canada, I would be perfectly willing to choose one which was shall I say not stable but which changed by reasonable amounts per period, so that it was continuous; but what does an export country do except try as best it can to rock with the punches? -- because it cannot control what its customers can do.

Q. Well, I was thinking of a rigid element such as freight rates might easily be, which would compel him perhaps to be a little more nimble than he would otherwise be in skipping from one thing to another?

A. I certainly have no wish to see freight rates made any more rigid than it is possible to do, but I think I did suggest that it was a problem of the adjustment of the whole protected sector of Canada and not of the railways only.

MR COVERT: Q. Now would you turn to page 17773? Just previously you had been discussing the east-west traffic situation in both Canada and the United States, and you were asked if you knew of any case in which the national policy of Canada had tended to force trade in east and west channels, and you said:

"Yes, I think there is one case. As a result of national pressure, the port of Portland, which had been used by the Grand Trunk as its winter port, was abandoned in favour of Canadian Atlantic ports."

And you say:

"The Maritimes, however, notwithstanding that they were the beneficiaries of this abandonment and re-routing, have complained and are complaining that they are suffering because the tariff policy forces them to look to Central Canada for their markets and their supply of manufactured goods."

Now, let us assume that what you say is correct there---

A. I think it is, sir.

Q. Yes, that the Maritimes are complaining in this fashion; does that have anything to do whatever with the question of Portland, Maine? Assuming that Portland, Maine, had still continued as the winter port of the Grand Trunk, has that anything to do with them suffering because the tariff policies forced them to look to Central Canada for their markets? I just do not understand.

A. Well, I suppose there is a connection in this sense, that if you transfer from Portland, Maine, which is

the closest point to Montreal, to Saint John and Halifax, you do so substantially on national grounds.

Q. Yes?

A. Now, if you benefit by a national policy, perhaps you have got to take the other side of it too.

Q. No, but I said, Professor McDougall, if they had not changed---

THE CHAIRMAN: If who had not changed? It was the railways that changed, was it not?

THE WITNESS: The railway did in fact change, yes.

THE CHAIRMAN: Q. Yes, but did you say that all this was substantially for national interests?

A. I think so.

Q. Was it not also to capture the traffic?

A. No, because the traffic would move by one winter port or the other. It is merely a question of which winter port you use.

Q. You mean, then, that the C.P.R. could go to Portland on its own line; is that it?

MR COVERTY: No, it is the Grand Trunk.

THE WITNESS: Portland was a Grand Trunk line.

THE CHAIRMAN: Q. It was Grand Trunk?

A. Yes.

MR COVERT: Q. But I say if the change had not been made how would that enter into it? Would that have made the complaint any different as far as looking to Central Canada for their markets and their supply of manufactured goods? I just did not follow, and I wondered if you could clarify it.

THE CHAIRMAN: I want to make sure I am following it. The change you refer to is the change from Portland to Saint John and Halifax?

MR COVERT: Yes, to Canadian Atlantic ports.

THE CHAIRMAN: And that was brought about by freight rates which would meet the traffic going the other way; is that it?

MR COVERT: I am not sure whether it was brought about that way.

THE CHAIRMAN: I would like to know that.

MR COVERT: Q. Do you know, Professor McDougall?

A. Well, as I remember the situation, it was about 1923 that, once the Canadian National became a Government-owned project, the port of Portland, which had been its outlet from 1860, became shall I say unacceptable, and it has not been -- well, I think for a year or two it may have had some minor use during the war, but substantially it has been for Canadian traffic a dead port since 1923.

THE CHAIRMAN: Q. Then the ports which benefited by that in Canada are---

A. Are Saint John and Halifax.

Q. In Saint John is it a fact there that that means principally the Canadian Pacific Railway?

A. Oh, yes. I should think it has reacted more to the benefit of Halifax than of Saint John, but I am making a guess there; I have not checked the facts; I just do not know the facts.

Q. Are the rates, then, which have turned the traffic in those directions the rates set by this conference of what-do-you-call-it?

A. I do not think it is a question of rates.

Q. Canadian Freight Association. I beg your pardon?

A. I do not think it is a question of rates; I think it is just a matter of direction of traffic. Perhaps the Canadian National will correct me, but that is my understanding of it.

Q. I thought we had been told that these low rates

which permitted the traffic to go out by Canadian ports was something done in the national interest?

A. Well, there are such rates, yes, but what I was referring to---

Q. I was referring now to Halifax and Saint John.

MR EVANS: They are related; the rates to Halifax and Saint John are related to the rates to the United States Atlantic ports.

THE CHAIRMAN: Are they not related by conference between the United States railways and the Canadian railways?

MR EVANS: Well, to some extent they may have been, but---

THE CHAIRMAN: I think to a large extent.

MR EVANS: Well, the Interstate Commerce Commission certainly recognizes the right of Canadian railways to make their rates to their Canadian Atlantic ports on no higher basis, although there is a longer distance, than rates would be moving from Canadian points to the United States Atlantic ports, and that we said was in the national interest, since it did provide benefits to the Maritime Provinces.

THE CHAIRMAN: I am not saying that it was not in the national interest, but I am looking for the motives, the reasons for it. Was it a sacrifice made by the people of Canada generally in the national interest, the people of the Maritime Provinces? Would you put it that way?

MR EVANS: Well, I venture to say this, that undoubtedly the Canadian railways got a longer haul on traffic, but I think it is only fair to say that they get very low rates for the additional distance they must haul the traffic, because they must not exceed the rates to a much less distant United States Atlantic port.

THE CHAIRMAN: They must meet those rates. If in turn the Canadian railways were to lower their rates, they would immediately be met by still lower rates in the United States.

MR EVANS: Yes; you would then have port competition, which we could not afford to---

THE CHAIRMAN: Yes; I found that out a long time ago in another connection.

MR COVERT: Q. What I was trying to bring out, Professor McDougall -- I am sorry if I am not clear on it -- I would suggest that the complaint that you refer to has nothing to do whatever with the situation that you are dealing with, in other words what you say is that national interest, because -- perhaps I could put it this way, to put it plainly, that they complained about the use of Portland, and as a result of complaints they used the Canadian Atlantic ports?

A. I think that is a fair statement of the facts.

THE CHAIRMAN: Who complained about it?

MR COVERT: The public, sir, generally, I think, in the Maritimes.

THE WITNESS: The eastern public, yes.

THE CHAIRMAN: Oh, well, yes, Halifax and Saint John complained; I know that.

MR COVERT: Q. But that has nothing whatever to do with the complaint, because of tariff policies forcing them to look to Central Canada for their markets, because if Portland were still used they would still have to look to Central Canada for their markets. I do not think there is any connection between the two, is there?

A. Well, let me put it to you this way, sir---

Q. Well, is there a connection?

A. I believe there is, yes.

Q. Well, let us have it?

A. I said both of these are aspects of national policy.

Q. Yes?

A. Now, then, in relation ---

Q. When you say both of these, you mean?

A. The movement of the ports and the tariff.

Q. Yes.

A. Now then, the Maritimes definitely have benefited.

THE CHAIRMAN: Q. And the tariff, do you mean---

A. And the tariff, the customs tariff.

Q. Yes?

A. Now then, I have myself many strong reservations about the customs tariff, but I say if you are going on the argument of national policy to demand that traffic shall move through the Canadian Atlantic ports, then the ground is cut from under you when you start to complain of other aspects of national policy.

MR COVERT: Q. And that is the way you hook them up?

A. Yes.

Q. You cannot complain of one and not complain of the other?

A. If you are going to start to recast your national structure, then you have got to toss it all in the pot and start afresh.

THE CHAIRMAN: Q. Do you mean to say, then, that probably the provision of rates which brought traffic out through Saint John and Halifax led to the demand then for goods to come back from the Maritimes into this preferred area?

A. No. I think Mr. Covert is correct in this sense, that even if the traffic still moved through Portland, if

the Canadian tariff were not changed---

Q. The Canadian tariff?

A. If the Canadian customs tariff were not changed, then there would be the pressure of that tariff toward a movement of manufactured goods into the Maritimes from Central Canada rather than from the New York-Philadelphia-Boston area.

COMMISSIONER INNIS: As a matter of information, do you know, Mr. Evans, whether the ocean rates to Atlantic coast ports have a differential over New York?

MR EVANS: Well, there are differentials, very small differentials, as between New York and Baltimore and Philadelphia. Just what those are I do not know, but the Canadian Atlantic ports are tied to one or the other.

COMMISSIONER INNIS: Not Boston?

MR EVANS: I do not think so. The rates to the Canadian Atlantic ports are based on New York. Baltimore is slightly under the New York rate.

COMMISSIONER INNIS: You mean the Canadian ports are the same as New York?

MR EVANS: The same as New York.

THE CHAIRMAN: Q. Will you tell me this, since you have introduced the customs tariff -- I will ask you this question: Are you telling us that these ports of Saint John and Halifax benefit now by importations into Canada according to the way the customs tariff now is, or are you saying the contrary?

A. I had not said that, although I believe it is the fact.

Q. It is a fact?

A. That there are differences in the application of the customs tariff, if imports move through Canadian ports.

Q. In fact are they moving in a way satisfactory to

Halifax and Saint John, from the United States or from Europe into those ports?

A. As to whether it is satisfactory---

Q. I ask you that because they are not moving from the middle west United States into Alberta in a way satisfactory to Mr. Frawley, for instance.

A. I think you will have to put that question to provincial counsel, sir; I just could not answer.

Q. But you started to talk about customs tariff and so on. All right, never mind.

MR COVERT: Q. At page 17775 you were referring to the railways running through this unproductive area north of the Great Lakes, I think?

A. Yes.

Q. And you said that the railways, not the economy in general, have to carry the burden of the cost of running through that area?

A. Yes.

Q. I just wondered, ordinarily if the railways bear it they must pass it along to the economy to bear, or would you say that that was perhaps one of the reasons that the railways have not been able to get sufficiently high rates, and that is the reason you say that the railways bear it rather than the economy?

A. Well, what was in my mind was this, that rates normally have been made using Winnipeg as taking the same rate from the east as Missouri River points, and from Winnipeg to the coast the same as those Missouri points to the Pacific Coast U.S.; that therefore when you make an equivalent rate and you do not have the local traffic upon the line, I think I can say with reasonable justification that the burden, such as it is, has been borne by the railways, and that because---

Q. Unless they pass that burden on to other parts?

A. Well, how do they pass it?

Q. Well, I say unless they do?

A. Oh, yes.

Q. You say they do not?

A. I say that, having looked at the earnings made by railroads at various periods, I think that they have been slightly below rather than above the United States level, yes.

Q. The earnings of---

A. That the earnings of Canadian railways---

Q. Does that mean, for instance, that the earnings of the Canadian Pacific---

A. Per cent upon its investment.

Q. ---have been lower?

A. Yes.

Q. Than the earnings of roads in the United States?

A. On the average, yes.

Q. On the average?

A. Yes.

Q. Then at page 17777 you made a statement near the bottom of the page:

"They have proven themselves capable of doing this, and with the lowest charges which exist in any modern nation."

A. Well, it is clear from what has happened, as has been put before this Commission, that the charges in Canada are now lower than in the United States. Charges in the United States are in their turn lower than in England or in any country I know in western Europe.

Q. I just want to find out what you are saying, Professor McDougall. Are you saying that---

A. Rates per ton mile---

Q. Rates per ton mile?

A. Yes.

Q. Are lower in Canada than in any modern nation?

A. Yes.

Q. That is what you mean, per ton mile?

A. Per ton mile, even after adjusting for average length of haul -- that is, a fully compensated figure, Canada is still lower.

Q. Than any modern nation?

A. Yes.

Q. You have made a study and found that out?

A. Yes.

Q. Now I turn to page 17796.

(Page 18012 follows)

Starting at the top of the page, I read:-

"The demand for transport on goods of high value is likely to be such that no rate increase which has been suggested would be likely to change the volume of movements, because of the relatively small proportion of the selling price of those goods that is represented by cost of transport. The demand for transport for low value goods is such that any increase in the cost of transport then may easily reduce the movement to a mere trickle because of the relatively large proportion of the selling price of these goods that is represented by cost of transport."

I just wanted to be clear on that.

A. Might I make a suggestion?

Q. Yes.

A. This is, I think, as I remember stating it - it would have been better had I stated on the fifth line from the bottom:-

"The demand for transport of low value goods is such that any major increase in the cost of transport...."

I would just put in that one word "major".

Q. Yes. Now then, you seem to recognize there that any major increase in the cost of transport may easily reduce the movement of low valued goods to but a mere trickle.

A. It is possible. You will have to know that, when making a study of commodity by commodity.

Q. Yes.

A. But I think that all such things as sand and gravel,

1. The first part of the paper is devoted to a general

discussion of the problem and the methods used.

2. The second part is devoted to a detailed

analysis of the results obtained.

3. The third part is devoted to a comparison

of the results with the theoretical predictions.

4. The fourth part is devoted to a discussion

of the experimental errors and the conclusions.

5. The fifth part is devoted to a summary

of the results and the conclusions.

6. The sixth part is devoted to a discussion

of the experimental errors and the conclusions.

7. The seventh part is devoted to a summary

of the results and the conclusions.

8. The eighth part is devoted to a discussion
of the experimental errors and the conclusions.

9. The ninth part is devoted to a summary
of the results and the conclusions.

10. The tenth part is devoted to a discussion
of the experimental errors and the conclusions.

11. The eleventh part is devoted to a summary
of the results and the conclusions.

12. The twelfth part is devoted to a discussion
of the experimental errors and the conclusions.

where you are continually competing against a relatively local self-sufficiency, and that on low rates you may be able to : set up one big pit and make substantial economies in it and pay whatever charge is levied.

Q. Yes.

A. Whereas, if you have a high rate, you might just wipe that pit out altogether.

Q. At page 17797, you are referring to the cost of the stove manufacturer from Sackville, and you said: -

"If they were charged the full average cost on incoming and outgoing freight, they would probably lose a large part of their present market."

Now, I just wondered what you meant by the full average cost of ingoing and outgoing freight. Do you mean that if they did not have the cost of service?

A. We are discussing here the cost of service principle as enunciated by British Columbia?

Q. That is right.

A. And what I said was that the inbound rate on the iron from the Sault, and the outbound rates on the stoves were both of them tempering the wind with the shorn lamb; and if you put the full average cost upon them, you might make stoves some place else besides Sackville, New Brunswick.

Q. You say they would probably lose a large part of their present market?

A. Yes.

Q. That would indicate, it would seem to me, that you must feel that the rates charged on inbound, on raw material, and on outbound finished products are a long way from the true cost of service?

A. From the full cost; I believe so, yes.

Q. You believe so?

A. Yes.

Q. Have you any idea how far away they are?

A. No. I looked at the rates as they are produced here.

Q. How did you test them? That is what I would like to find out.

A. If you are going to make a full test - -

Q. Did you test them? Did you test these rates?

A. I checked the rate per ton mile as it came through on the floor here.

Q. You checked the rate per ton mile as it came through on the floor here on the inbound and the outbound in this case?

A. Yes.

Q. What yardstick did you use?

A. Well, having the average rate per ton mile of all traffic, and recognizing that that rate was - that that average was depressed as against any normal conditions, I said this was a remarkably favourable rate compared with other rates.

Q. In other words, you found the rate on the inbound material to the plant at Sackville, was, as you put it, a favourable rate?

A. Yes.

Q. And that its yield per ton - -

A. Per ton mile, I think is a shade better.

Q. That its yield per ton mile was lower than the average?

A. Yes.

Q. And that the outbound rate you found the same?

From the High Court, I believe so.

I am not sure about the date.

But I am not sure about the date.

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A. On your inbound commodities you can load heavily.

Q. Yes.

A. And therefore your ton mile is a good indication. But when you come to take outbound traffic, you must use at least a combination of the carmile earnings and the ^{net} gross/ton miles.

Q. You applied both of those tests to the outbound from Sackville?

A. Yes.

Q. Did you test them for any distance?

A. To the west particularly.

Q. And you found that in both of those cases they were below the average?

A. What I did was to take, as nearly as I could, the weighted results, because if you are going to come to a pure cost of service basis, you are not going to make a test only under the value of service principle; but you will take varying rates as between commodities.

Q. Did you test them separately, and then together?

A. I tested them together.

Q. But not separately?

A. You have no test until you put them together.

Q. But did you test them separately?

A. Yes.

Q. And did you test them together?

A. It was only when they were together that you had a proper test.

Q. Did you test them together?

A. Yes.

Q. Very well. And you say that as a result of testing them together, the combined result was considerably below the average?

A. Yes.

Q. That is, when you say "below the average" you are referring then to what?

A. Below the average normal return on that volume of traffic.

Q. And it is on the basis of a conclusion of that kind that you say that they are not bearing their full average cost; and that if they were, they would probably lose a large part of their present market?

A. Yes. Now, I cannot forecast what would happen were Mr. Brown's rates put into effect.

You might have results with other costs such as wages. You might have many things. But if those other things remained relatively constant, then the market would shrink.

Q. And at page 17800 where you are still dealing with the same subject of cost of service, you suggest that any major alteration in it would involve a very major reorientation of the economy. You say:-

"The whole economy has been built up on a rate system based on the value of service principle, and I would expect that any major alteration in it would involve a very major reorientation of the economy".

A. Yes.

Q. Now, I would gather this; that what you in effect say: that there would be a much difference in the rates, if they were on a cost of service basis than the rates which would exist if they were on a value of service basis?

A. Yes.

Q. And that the rates would be very different?

A. I believe so.

Q. That is what you mean, and that would mean a major reorientation of the economy?

A. Yes, too big for anybody safely to forecast. All you know is that it would be big.

Q. I wonder how you arrived at that conclusion without having any idea as to what rates would be involved if they were put on a cost of service basis?

A. I must say that I thought first of the grain rates.

Q. Yes.

A. And it seemed to me that there would be a very great change if you put them on a full average of all-in cost of service.

Q. Yes.

A. And I thought also of the rates on other heavy commodities, without holding myself out as an expert in freight rates. I think it is a reasonable statement.

Q. So that is the way you arrive at the conclusion. You believe that if you should put sand, for instance, on a cost of service basis, there would be so much difference in the rate that it would not move?

A. It certainly would not move in its present volume.

Q. That is your view?

A. Yes.

Q. But you have not made any study to bear that out?

A. Oh, no. I would want two years if I were asked to do it.

Q. You would be surprised, though. I think you reject the cost of service principle entirely, and you would be surprised if you found that, generally speaking, the value of service coincided remarkably with the cost of service.

THE CHAIRMAN: Found out what?

MR. COVERT: Q. If you found that, generally speaking, the value of service coincided remarkably with the rates under cost of service.

A. Oh, that seems to me more than any statistics I have ever seen would bear out, and I have given a lot of time to analyzing statistics of railway operations. There I can claim to be an expert.

Q. You can claim to be an expert?

A. Yes.

Q. Those statistics which you have seen, you say that they would indicate that there would be a vast difference, Professor McDougall between the rates under cost of service and value of service?

A. Well, if you are going to have a cost of service basis, purely - -

Q. You could not answer my question in any other way?

A. Not and be sensible, no.

Q. Very well, let us try it again. Would the reporter please read the last question?

THE REPORTER:-

"MR. COVERT: Q. Those statistics which you have seen, you say that they would indicate that there would be a vast difference, Professor McDougall, between the rates under cost of service and value of service?"

A. Yes.

Q. I see.

A. Might I explain?

Q. If we could only start out with a yes, no, or a maybe, or perhaps with a "I can't answer it"; however,

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FROM THE FIRST SETTLEMENTS TO THE PRESENT TIME

BY JAMES M. SMITH

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let us go on.

A. If you have a cost of service basis, you have, in a sense, one rate.

Q. For what?

A. For anything. You have a terminal cost, and then you have a cost per mile thereafter, regardless of the product.

THE CHAIRMAN: Regardless of what?

A. Regardless of the product.

MR. COVERT: Q. Is that your understanding of the British Columbia cost of service principle?

A. Yes. This is an adjusted figure of cost, they admit, to compensate for differences in car loadings. But the difference is in actual outlay of money to provide the service. It has nothing whatever to do with the relative demand for the product, or its value, or anything else.

I think I am being fair in this. They say there might be a spread as high as eight or ten to one between the rates on things which loaded in one fashion as against the rates on things loaded in another.

But where you have the cost of service basis, you are loading on each product, regardless of its value, the full all-in cost.

Q. By "all-in", you mean all-inclusive?

A. By all-in I mean all-inclusive, such as depreciation, return on capital, income tax, and everything; whereas, under value of service, you are looking to see what will move and how it will move; and I believe there would be a very big difference between the one and the other, yes.

THE CHAIRMAN: We shall now take a recess.

...SHORT RECESS

(continued)

--- On resuming:

MR. COVERT: Would you turn to page 17841 of the transcript of evidence, Professor McDougall?

A. Yes, sir.

Q. Now, when you say at the bottom of the page there:

"I would think that at today's costs a railway property equal in capacity to that which the Canadian Pacific has built up would result in a rate base which is much higher than is represented by the depreciated book value of the existing property."

You probably have not really made a study of that, perhaps you have not checked, for instance, the historical cost and the depreciation making up what they suggest might be a fair rate basis.

A. This is a statement which is based upon the movement of prices since Canadian Pacific began, and obviously I am not an engineer,--

Q. And you are assuming their figures are correct?

A. I am trying to compensate also for those changes which come in relative technical efficiency, that is, even though some grading had a high initial cost the increase in the value of grading on a reproduction basis might be less now than it was then, or perhaps I should change that, it would not have increased proportionately with the price level because there had been special improvements in moving earth. I think also of some kinds of property which might not now be replaced in kind but would be replaced differently. I am trying to make all those corrections, rough, it is true, but still to make them, and I still come up with that statement.

Q. Would you turn to page 17847 of the transcript where you say at the bottom of the page:

"that the railways no longer have a monopoly of land transportation. Therefore there is no longer any problem of a potentially excessive general level of rates."

Now, have you made any studies at all as to what portion of the traffic the railways still have a monopoly on, or, upon which they still have a monopoly?

A. Well, you have a varying situation.

Q. You run from those things which they have lost through to those which are still rail bound.

A. Obviously it is not as to any particular commodity, it is at least as to the product of commodity and distance of movement.

Q. Would you think they still had a monopoly on a large volume of the traffic?

A. Yes, I would think so, just because their costs are so low, but a diminishing proportion of the total.

Q. You feel that it is a diminishing proportion of the total?

A. Yes.

Q. Now, there was one statement I thought perhaps you might want to give some more consideration to, it appears on page 17856 of the transcript of evidence and again on 17857, where you were discussing the over-investment in cars and you intimated that in that case the regulatory body would say that the rate base was too high and that these cars should be excluded.

A. Excluded from the rate base, yes.

Q. Do you think that that should be a factor which the Board should take into consideration?

A. Well, it would have to be a gross over-investment, that is, I would not think it proper to exclude it if it was merely a cyclical drop. I am trying to exclude cyclical influences in that answer.

Q. It would be putting the regulatory body in almost a managerial capacity?

A. No, not quite. It would have to make an estimate and prove it that this was an over-investment which a prudent management would not have made.

Q. Well now, Professor McDougall, on page 17858 of the transcript, you were asked by Dr. Angus:

"Q. Do I gather that the regulatory board would not step in except in two situations -- one, if the net earnings of the whole system were above what was permissible. . . ."

THE CHAIRMAN: Did you say 'permissible'?

MR. COVERT: Yes, 'permissible'.

". . . and, two, if an individual rate were discriminatory?"

And then your answer to that was 'yes'. And then you were asked:

"Q. And it is under those conditions that you want the Crow's Nest rates put at the disposal of the Board?"

And your answer was again 'Yes'?

A. Yes.

Q. I just wanted to know if you want to add anything further to that.

THE CHAIRMAN: Is there anything more said about the meaning of the word 'permissible'?

MR. COVERT: Possibly the professor might want to define it. I gather that as long as the net earnings for the whole system were not in excess of what they were

permitted to earn by the calculation of the rate based on the rate of return,--

THE CHAIRMAN: Who would determine that?

A. Would that not be the determination of the Board? The Crow's Nest pass rates of course would be directly comparable with those of other products of similar rough value and movement, that is, rates on grain should not be discriminatory against grain.

THE CHAIRMAN: Rates on grain should not be discriminatory,--

A. Rates on grain should not be discriminatory against grain by comparison with equivalent products moving equivalent distances.

THE CHAIRMAN: Q. What do you mean by 'equivalent products'?

A. I am hard put to find any particular example. What I mean is a product of nearly the same value and having the same loading characteristics.

MR. COVERT: Q. I suggest, Professor McDougall, that perhaps the Board would be hard put to find something similar?

A. Well, they might have difficulty, but surely every case of classification involves just that kind of consideration.

THE CHAIRMAN: Isn't that a new kind of discrimination that you are creating there?

A. I don't think so, sir.

Q. So far, we have had discrimination between shippers and localities.

A. This is a discrimination between products.

Q. I say it is a new kind of discrimination?

A. It may be new here, I do not think it is new in discussion of the topic.

Q. Are you just coming back to a basis of some comparison to fix just and reasonable rates by saying: "Well, another product in another part of the country gets another rate which is lower than mine, therefore, mine is not just and reasonable." Is that what you mean?

A. Yes, something of that kind.

Q. You are not much further ahead than we are today, then, at the present time?

A. Well, if your grain rates are as far out of line with other products.

Q. You are talking of the rates on grain and flour, the Crow's Nest Pass rates?

A. Yes.

Q. And you would suggest that those shippers be left in this position, that they have no complaint unless they can show that some other shippers in some place else in Canada on similar goods are receiving a lower rate?

A. If that happened, then they would have a claim of discrimination.

Q. You have thought this out, of course, but you are not able to tell us yet what similar goods would be, that is, what basis of comparison they could make. How would they voice their complaint?

A. If it were Mr. Jefferson who was here, I am sure he could answer at once. It is simply a lack of detailed knowledge that prevents me from answering.

Q. Well, it is much more than detail because you propound a doctrine there, you say that is what ought to be. Well, then we must see what the consequences are.

MR. EVANS: I just want to suggest that grain is classified, its classification is eighth class.

THE CHAIRMAN: Q. What other commodities are in that class?

MR. EVANS: There are other commodities, but the whole method followed in classifying different products is based on the analogy rule. My friend, Mr. Sinclair, tells me that potatoes are also eighth class and rough vegetables are eighth class. The analogy rule would be called into play.

THE CHAIRMAN: You might say that the grain shipper might complain that the potato shippers are getting a more favourable rate in eastern Canada than he is getting?

MR. EVANS: He might say that or he might see that the true analogy lay elsewhere.

THE CHAIRMAN: I know, but you are giving me the classes, the possible solution. Do you think that would be a reasonable way to leave the Act?

MR. EVANS: I was going, at the conclusion of Mr. Covert's examination perhaps to give your lordship something further than I gave you this morning. While I am on my feet may I say this, that we do not ask for any change in the Act other than that set forth in the brief; in particular, we do not ask that the suggestion this morning, that the only regulation to be left in the Act should relate to the two things of which Mr. McDougall speaks. Now, that is not to say that I do not feel they can be defended, I do, I simply say we do not ask that that be done.

There is a good deal to be said for relaxation, and the Commission will recall that our brief argues that, if there is to be a change, a substantial change, in the scheme of regulation, it ought to be in the direction

of relaxation rather than in the direction of greater or more rigid regulation.

THE CHAIRMAN: It may be that in view of the product that Mr. McDougall has chosen as an example we are getting too close to the Crow's Nest Pass arrangement, which is to come on later.

MR. EVANS: Yes. I wonder if it was chosen by him or by Dr. Angus.

MR. COVERT: Dr. Angus.

COMMISSIONER ANGUS: I wonder if we are not talking a little at cross-purposes. I understood you to say that there was so much competition today that the Board could limit its control to two things, one, that the aggregate net revenue of the railways should not be too high and, two, that rates should not be discriminatory between themselves.

A. Yes.

Q. In fact, I understood you therefore to suggest that you would be getting rid of individual rate controls and also of classifications, that is to say, that there would not be compartmentalized control of particular rates in addition to this control of the aggregate.

A. I had not thought of abolishing the classifications at all.

Q. But the language you used seemed to suggest doing it. You were limiting control so narrowly that you seemed to me to have swept out the classifications with the other controls.

A. I just do not see how you can have a value of service rate structure without classification.

Q. Well, you would have classifications that were purely at the option of the railways, that is to

say that they could change according to their ideas of value of service, or you could have classification control by the Board. Now, it is the control by the Board. not control of the classifications, that I thought you were wishing away.

A. I was not intending that, sir, no. Classifications presently are worked out by the conference method between railways and shippers and are brought to the Board substantially as an agreed solution. I think that is valuable enough to retain. I had not thought at all of washing them out.

COMMISSIONER INNIS: In your reference to the values of commodities it seems to me you are getting close to Mr. Frawley, that is, discrimination as between commodities ^{you are complaining about,} is what/Mr. Frawley, in connection with the livestock industry.

MR. FRAWLEY: Yes, the lack of proper relationship between those two rates.

MR. EVANS: Oh, yes, Mr. Frawley goes much further than that. He says 'I fix the relationship on the input-output ratio without regard either to cost of service or value of service.'

COMMISSIONER INNIS: I was wondering whether Mr. McDougall would include this.

THE WITNESS: No, I am letting the value of service principle ride without Mr. Frawley's limits on it.

COMMISSIONER INNIS: You would not go any further in defining or interpreting it?

THE WITNESS: No.

MR. COVERT: Now, just three other little points in the evidence, -- one on page 17873 of the transcript at the top of the page. You say there:

"There is competition between the two railways.

I know, from talking to small shippers, that this gives them a leverage which no regulatory body could give."

You feel, Professor McDougall, that there is really competition between the two railways, the Canadian National and the Canadian Pacific?

A. Oh, yes.

Q. Could you give us some examples of that?

A. Well, it is from talking to different people some in Kingston, some elsewhere, who have used the shipping of their traffic to get what they thought they ought to have in service.

Q. It is a service competition?

A. Oh, yes.

Q. That is the kind of competition to which you are referring?

A. That is the kind of competition that I have most seen, and had related to me by shippers.

Q. That is the kind of competition you refer to, service competition?

A. Yes.

Q. Is that the only competition to which you refer there?

A. Well, I know from reading though I have not met it in my own experience that very frequently the railways differ between themselves inside the conference as to what they shall do about rates; they do in fact each maintain the liberty of independent action and that some cases do occur from time to time where one railway will say 'Well, this is sufficiently in my interest that this is what the rate is going to be.' And therefore, I think

that having two people to play one against the other does have its effect on rates as well as upon service. But as I say I have not managed to find one case and have it related to me by the man who is actually in the middle.

Q. But in that case you do not suggest they come out with different rates?

A. Oh, no.

COMMISSIONER INNIS: Would you object to the word 'duopoly' to describe the railway situation?

A. No.

MR. FRAWLEY: That situation is limited to a competitive point, again, not where you are on one line of railway like Lethbridge.

A. Except as you have market competition.

THE CHAIRMAN: Market competition between shippers or between railways?

A. Well, if a shipper who is located on the Canadian Pacific line at Lethbridge, as Mr. Frawley says, and there is another shipper on the Canadian National line, and they are trying to sell in a common market --

THE CHAIRMAN: Both railways going to the same market?

A. Yes. Then the railways themselves are in there, whether they like it or not, and they are going to try to see that conditions exist so that the producer on their line whose revenues they get will have a good break in that market.

Q. Do you mean a lower rate than the other railway offers him?

A. Well, they may not be able to get a lower rate, but they will at least see that he is not unduly prejudiced, and they must see to it for their own private interest.

Q. Then they both must see to it?

A. Yes.

Q. That is a happy way for the shipper to be, isn't it?

A. Oh, quite.

MR COVERT: Q. Now, Professor McDougall, at the top of page 17875 Commissioner Angus put to you:

"The more strictly regulated a private interest is the more advantages there would be?"

And you answered:

"I would think so, yes."

COMMISSIONER ANGUS: There seems to have been a mistranscription for "fewer" the second time it is used.

THE WITNESS: "The more strictly regulated a private interest is the fewer advantages there would be?"

MR COVERT: Yes, I thought that should be corrected.

COMMISSIONER ANGUS: I put in a correction at the office.

MR COVERT: Q. At the very bottom of the page -- and this is the last matter I want to deal with with you, Professor McDougall -- you say:

"Comprehensive regulation was one thing when railways had a monopoly of land transport; it loses

much of its justification when railways are exposed to competition on all their high-grade traffic."

I just wanted to find out if you are of the view that they are exposed to competition on all of their high-grade traffic?

A. "All generalizations are false, including this one." There must be some high-grade traffic on which they are not, but it is narrowing all the time.

Q. Do you think it is very little?

A. No.

Q. That is all, thank you.

THE WITNESS: ~~He~~ Thank you, Mr. Chairman.

THE CHAIRMAN: Thank you, Mr. McDougall.

Are you through, Mr. Evans?

MR EVANS: I have no re-examination, my lord.

THE CHAIRMAN: Thank you, Mr. McDougall.

Who is the next witness?

MR SINCLAIR: Mr. P. C. Armstrong, my lord.

P. C. ARMSTRONG, Called.

EXAMINED BY MR SINCLAIR:

Q. What is your occupation, Mr. Armstrong?

A. I am Economic Consultant of the Canadian Pacific Railway.

Q. Would you describe briefly and outline your personal history and experience?

A. I was born and educated in the Island of Barbados. I came to the United States in 1901, where I became a construction engineer. I moved to Canada in 1906 and continued as an engineer in charge of various construction projects, in various parts of the United States and Canada, until 1913. I was works manager of the crane plant of the Dominion Bridge Company during the first World War, engaged in munitions production. In 1918, for reasons of health, I retired to a farm in the eastern townships of Quebec. Becoming^{interested} in the economic problems of agriculture, I may say because of very sad experiences in playing with the economics of agriculture personally, and as the result of long interest in economics in general, I devoted the next few years to intensive study in various fields of economics. In 1925 and 1926 I was Economic Adviser to the National Dairy Council of Canada. In 1926 I entered the service of the Canadian Pacific Railway as a part-time agricultural specialist. In 1928, 1929 and 1930 I gave almost all my attention to the study of the economics of production and distribution of wheat, visiting Great Britain and western Europe on several occasions and spending a great deal of my time in Western Canada. In 1930 I entered the full-time service of the Canadian Pacific Railway, with the title of Special Representative, and in due course became an economic adviser to the President. A few years ago I was appointed Economic Consultant.

Q. So would it be correct to say that your particular economic interest for many years was agricultural economics?

A. And especially the transportation and marketing, of wheat.

Q. And your interest in that has continued, and your study?

A. Very much so.

Q. Have you written on the subject of economics?

A. In 1929, in collaboration with Professor W. W. Swanson, then of the University of Saskatchewan, I published a book called "Wheat", dealing with the economics of wheat production and distribution. In 1934, in collaboration with Mr. F. E. M. Robinson---

Q. Who was he?

A. Mr. Robinson is a Master of Arts, Trinity College, Cambridge, and he is also the best amateur veterinary surgeon in Canada, and one of the largest ranchers in Alberta.

Q. And in collaboration with Mr. Robinson---

A. I published a book called "City and Country", dealing with agricultural economics in general.

THE CHAIRMAN: Q. What is the name of the book?

A. "City and Country." It is a book intended to point out that there has been too much neglect of the interest of the farmer in our modern civilization, with very sad results. Last year I published a book called "Two and Two", dealing with various current economic theories -- the only book on economics illustrated with comic cuts. I have also published many articles on various economic subjects, and especially on transportation.

MR SINCLAIR: Q. Now, what is the nature of your present duties, Mr. Armstrong?

A. I am engaged in constant study of current economic

problems of many types. The Canadian Pacific sent engineers in, placing at my disposal an office and a small staff -- a couple of stenographers, to be precise -- and giving me the facilities with which to carry on economic research, and I have a large acquaintance among the economists of this and other countries and carry on a great deal of correspondence and discussion with them, and I try to keep myself informed about economic developments in general, questions of foreign exchange, anything of the kind -- whatever is the current economic problem of the time -- and the company apparently is quite willing to have me go on acting as this sort of student, rather advanced in years, on condition that my services are available to the officers of the Canadian Pacific at all times as economic consultant.

Q. Now, Mr. Armstrong, you have come to give evidence before this Commission, with particular relation to the matter of grain. If as a result of abolishing the statutory fixing of rates on grain in Western Canada and placing such rates under the jurisdiction of the Board of Transport Commissioners these rates should be increased, who in your opinion would bear such increase?

A. It is never possible to say with complete certainty and exactitude who bears any special item in the total cost of any part of the production and distribution of any goods. In the end all the cost of wheat is borne by the ultimate consumer.

Q. And when you say all the cost, you underline the "all"?

A. All.

Q. You emphasize the "all"?

A. All -- every item that goes into the cost, because he is the individual who buys and eats bread, and when he

bought the loaf of bread he paid all the cost that had gone into the production of it, the production and distribution of it.

THE CHAIRMAN: Q. Does that follow the wheat up to the foreign consumer of bread?

A. It does indeed, sir, The price to the consumer is set by a complex of forces.

MR SINCLAIR: Q. A complex of forces -- would you explain, please?

A. Well, it is set by the relationship between demand and supply -- I hesitate to say so -- by the comparative elasticity of the demand, and by even such questions as psychology; mass psychology will affect it. We have the good or bad state of international exchange of currencies. All these factors enter into the setting or the establishing of the price for a commodity.

Q. And when you refer to a complex of forces, you are taking into account these various factors that you have mentioned and others, I presume?

A. Yes. In the case of a commodity produced and consumed on a large scale in many parts of the world -- because, after all, something close to 1,800 million people at least eat wheat to some extent, most of them---

THE CHAIRMAN: Q. You mean billion, don't you?

A. 1,800 million.

Q. I beg your pardon.

A. Yes, 1,800 million eat wheat to some extent, most of them as their staple food as a matter of fact, and in addition to that wheat is produced in dozens of countries by hundreds of millions of farmers. So the process of establishing the price of wheat is so complex that it is quite impossible to say with absolute precision who benefits from some increase or reduction of some special item in the total

cost in every specific case.

MR SINCLAIR: Q. Now, if there is difficulty in saying with exactitude or precision who bears the cost in any or every specific case, is there any general principle to guide us in this problem?

A. Yes. Broadly speaking, when the buyer has a definite advantage in the market he can take advantage of any reduction in costs. When the seller is in the saddle he can retain any savings in cost of production. The extent to which either uses his advantage will depend on how well informed and skilful a trader is.

Q. How would this apply on the export trade in wheat ? How would that principle apply?

A. With special force, because this trade is carried on between large buyers and sellers with great experience and much trading skill. That was always the case with wheat, and is more than ever the case in these days of bulk trading between nations. In such a case the principle will apply with considerable force almost completely. It will almost completely be the case that in a buyer's market the buyer will collect any savings that are made, and in the seller's market the seller may be able to retain it, and may desire or not to retain it.

Q. Now, with a very simple illustration would you apply that principle?

A. Yes. Take the case of the Widow Jones. Now, I do not want anyone to think that this is an apocryphal case, though the lady's name was not Jones and she was not a widow, but this is a case to which I can testify from personal knowledge. This lady keeps a few hens and she sells eggs to the village storekeeper, and he is a hard-hearted buyer and the only buyer---

THE CHAIRMAN: Q. Could you tell us where this

1. The first part of the document is a letter from the President of the United States to the Congress, dated January 3, 1862. The letter is addressed to the Senate and the House of Representatives, and is signed by Abraham Lincoln. The letter discusses the state of the Union and the progress of the war against the Confederacy. It also mentions the Emancipation Proclamation and the importance of the Union's cause.

2. The second part of the document is a report from the Secretary of the War Department, dated January 10, 1862. The report is addressed to the President and the Congress, and is signed by Edwin M. Stanton. The report discusses the military situation in the South and the progress of the Union's army. It also mentions the importance of the Union's cause and the need for more resources.

3. The third part of the document is a report from the Secretary of the Navy Department, dated January 15, 1862. The report is addressed to the President and the Congress, and is signed by Gideon Welles. The report discusses the state of the Navy and the progress of the Union's fleet. It also mentions the importance of the Union's cause and the need for more resources.

4. The fourth part of the document is a report from the Secretary of the Treasury Department, dated January 20, 1862. The report is addressed to the President and the Congress, and is signed by Alexander C. Gibson. The report discusses the state of the Treasury and the progress of the Union's finances. It also mentions the importance of the Union's cause and the need for more resources.

5. The fifth part of the document is a report from the Secretary of the Interior Department, dated January 25, 1862. The report is addressed to the President and the Congress, and is signed by Caleb B. Smith. The report discusses the state of the Interior and the progress of the Union's land and mineral resources. It also mentions the importance of the Union's cause and the need for more resources.

6. The sixth part of the document is a report from the Secretary of the War Department, dated February 1, 1862. The report is addressed to the President and the Congress, and is signed by Edwin M. Stanton. The report discusses the military situation in the South and the progress of the Union's army. It also mentions the importance of the Union's cause and the need for more resources.

7. The seventh part of the document is a report from the Secretary of the Navy Department, dated February 5, 1862. The report is addressed to the President and the Congress, and is signed by Gideon Welles. The report discusses the state of the Navy and the progress of the Union's fleet. It also mentions the importance of the Union's cause and the need for more resources.

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lady is?

A. I am sorry---

MR SINCLAIR: On a farm in Saskatchewan.

THE WITNESS: I am sorry, sir, but it is not in the Province of Saskatchewan or in Alberta.

COMMISSIONER INNIS: Q. In Manitoba?

A. I refuse, sir -- I am sorry; I do not want to be in contempt of court, but I must not give away any further secrets.

THE CHAIRMAN: Q. Is she in Canada?

A. She is definitely in Canada.

MR FRAWLEY: But the hard-hearted buyer lives on St. James Street, I suppose.

THE WITNESS: No, he is the village storekeeper in the next village there, and no more hard-hearted than the merchants in the big cities, and he is the only buyer available to her. There is a perfect buyer's market; she has to take her eggs to this man.

THE CHAIRMAN: Q. Where is the buyer?

A. In the neighbouring village.

MR SINCLAIR: This is an illustration that he is using of a village storekeeper who buys eggs.

THE WITNESS: Now, she lives too far from the village to carry the eggs in herself, and her neighbour Smith charges her a cent a dozen for carrying them in. Now, this actually happened. The storekeeper managed to beat her down we will say to twenty cents per dozen. That was the bottom of the market. At any lower price she simply would not engage in egg production, and she told the storekeeper that -- "I will go no further down."

COMMISSIONER INNIS: Q. When was this, Mr. Armstrong?

A. That again is a perfectly genuine case that happened a couple of years ago, a few years ago as a matter of fact, in more depressed conditions than exist just now. Now, in order to help her, her neighbour Smith, the farmer, who takes her eggs in, told her that he would carry the eggs in for nothing. That was to help this poor distressed widow. Now, the storekeeper knows that the Widow Jones will sell the eggs for nineteen cents per dozen, because that is what she was getting, nineteen cents a dozen -- twenty cents at the store, less the one cent that neighbour Smith was charging her -- so as soon as he hears, if he does hear -- and you know how you hear these things in country areas -- that neighbour Smith has decided to bring the eggs in free, being a kind, generous fellow, he at once proceeds to offer her nineteen cents a dozen, quite convinced that if she would sell them for nineteen cents a dozen yesterday she will sell them for nineteen cents a dozen today, and she did, so that neighbour Smith made the kindly gesture of carrying the eggs in free, and it did not bring anything in to the Widow Jones.

MR SINCLAIR: Q. Suppose, to carry out this illustration, that there is another market---

THE CHAIRMAN: Q. Neighbour Smith was the railway, I suppose?

A. Well, I am sorry, sir, but it was just a farmer at this stage.

MR SINCLAIR: I will ask the witness to apply the illustration to wheat, if I might, sir.

THE WITNESS: If I might finish this one paragraph.

COMMISSIONER INNIS: To carry out the balance of this illustration, I asked the witness to suppose that there was another market.

THE WITNESS: Now, suppose that the Widow Jones finds another market, so that there is competition set up, or suppose the demand for eggs is such that the storekeeper feels that he would be wise to pay a little more to get more eggs. That is a seller's market. The Widow Jones got twenty-five cents a dozen, we will say. Now, neighbour Smith, knowing all this, raises the price of carrying a dozen eggs to two cents instead of one. He wants to get a little of the share of the increased prosperity. If the seller's market is sufficiently well established, Widow Jones can pay this two cents, but is in a position to make the storekeeper raise the price to twenty-six cents instead of twenty-five cents, to cover the added cost of the increased freight rate charge by neighbour Smith.

THE CHAIRMAN: We will adjourn now.

---The Commission adjourned at 4:45 p.m., to meet again at 10:30 a.m. on Wednesday, March 15, 1950.

A.R.

3-15-50

ROYAL COMMISSION
ON
TRANSPORTATION

EVIDENCE HEARD ON

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ROYAL COMMISSION ON TRANSPORTATION

WEDNESDAY, MARCH 15th, 1950

Index Page #115

MR. FRAWLEY: Filed:

Page

<u>EXHIBIT No.208:</u>	Statement reflecting an increase in rates going into effect on March 23, 1950, on Canned goods, car-loads, from Hamilton, Ont. - - - - -	18045
<u>P. C. ARMSTRONG</u> -	Recalled. Examination by Mr. Sinclair resumed - - - - -	18047
Noon adjournment - - - - -		18138
<u>P. C. ARMSTRONG</u> -	Recalled. - - - - -	18139
The Chairman:	Statement re importations of Canadian wheat - - - - -	18139
	Examination continued by Mr. Sinclair - -	18140
<u>EXHIBIT No.209:</u>	Map of Canada, marked out in zones, showing rates on grain and grain products - - - - -	18186
<u>EXHIBIT No. 210:</u>	Map of United States - 1947 Wheat Crop in 18 chief producing states, in millions of bushels - - - - -	18192
Adjournment - - - - -		18208

- - - - -

1. The first part of the report deals with the general situation of the country. It is a very interesting and informative study of the country's development. The author has done a great deal of research and has gathered a wealth of material. The report is well written and is a valuable contribution to the study of the country's development.

2. The second part of the report deals with the economic situation of the country. It is a very interesting and informative study of the country's economic development. The author has done a great deal of research and has gathered a wealth of material. The report is well written and is a valuable contribution to the study of the country's economic development.

3. The third part of the report deals with the social situation of the country. It is a very interesting and informative study of the country's social development. The author has done a great deal of research and has gathered a wealth of material. The report is well written and is a valuable contribution to the study of the country's social development.

4. The fourth part of the report deals with the political situation of the country. It is a very interesting and informative study of the country's political development. The author has done a great deal of research and has gathered a wealth of material. The report is well written and is a valuable contribution to the study of the country's political development.

5. The fifth part of the report deals with the cultural situation of the country. It is a very interesting and informative study of the country's cultural development. The author has done a great deal of research and has gathered a wealth of material. The report is well written and is a valuable contribution to the study of the country's cultural development.

ROYAL COMMISSION ON TRANSPORTATION

OTTAWA, ONTARIO,
WEDNESDAY,
MARCH 15, 1950.

THE HONOURABLE W.F.A. TURGEON, K.C., LL.D. - CHAIRMAN
HAROLD ADAMS INNIS - COMMISSIONER
HENRY FORBES ANGUS - COMMISSIONER

G.R. Hunter
Secretary

P.L. Belcourt
Asst. Secretary

COUNSEL APPEARING:-

F.M. Covert, K.C.	}	Royal Commission on Transportation
G.C. Desmarais, K.C.		
H.E. O'Donnell, K.C.	}	Canadian National Railways
H.C. Friel, K.C.		
F.C.S. Evans, K.C.	}	Canadian Pacific Railway
I.D. Sinclair		
C.D. Shepard	)	Province of Manitoba
M.A. MacPherson, K.C.	}	Province of Saskatchewan
F.C. Cronkite, K.C.		
J.J. Frawley, K.C.	)	Province of Alberta
F.D. Smith, K.C.	}	Province of Nova Scotia; Transportation Commission of the Maritime Board of Trade.
J. Paul Barry		
C.W. Brazier		
J.O.C. Campbell, K.C.		
	)	Province of New Brunswick
	)	Province of British Columbia
	)	Province of Prince Edward Island.

OTTAWA, ONTARIO.
WEDNESDAY, MARCH 15th, 1950

M O R N I N G S E S S I O N

MR. FRAWLEY: Before Mr. Sinclair proceeds with his witness, I should like to offer an exhibit reflecting the increase in rates which will go into effect on the 23rd of this month as a result of the recent order of the Transport Board. I do that simply to show the effect of a horizontal increase on the long haul. The statement is a very short and simple one. It shows the rates on canned goods in carloads from Hamilton Ontario to Montreal, Halifax, Winnipeg, Edmonton, Grande Prairie. In the case of Montreal it indicates an increase of 37%. The two rates I am comparing are the rates in effect on April 7, 1948, before the 21 % increase and the rate as it will be on March 23, 1950. The rate to Montreal was 35¢ and will be 48¢, an increase of 13¢ or a percentage increase of 37. The rate to Halifax was 61¢ and will be 86¢, an increase of 25¢, or an increase of 40%. The rate to Winnipeg was \$1.14 it will become \$1.60, an increase of 46¢ or 40%. The rate to Edmonton was \$1.98 and it will become \$2.78, an increase of 80¢ or 40%. The rate to GrandePrairie was \$2.31 and will become on March 23, \$3.25, an increase of 84¢ and still an increase of 40%. The rate to Vancouver was 96¢ . It will become - as it is now and has been for some time, and will so remain, ~ \$1.40 on March 23, an increase of 44¢ and a percentage increase of 46.

MR. COVERT: That will be Exhibit 208.

... <u>EXHIBIT 208</u> ...	filed by	:	Statement reflecting an
	Mr. Frawley	:	increase in rates going
		:	into effect on March 23,
		:	1950, on Canned goods,
		:	Carloads, from Hamilton,
		:	Ontario.

THE CHAIRMAN: Is there any explanation for the size of this increase?

MR. FRAWLEY: All I want to say is that you have an increase of 84¢ to GrandePrairie that is 40%. Your lordship understands that the general increase we have been speaking of since the 21% Case now totals, roughly, 40%, and that this 40% increase to Grand Prairie is 84¢. The same 40% increase to Halifax is only 25¢; the same 40% increase to Winnipeg is 46¢, to Edmonton it is 80¢ and to GrandePrairie, Alberta, it is 84¢, about double the next nearest rate that I take, namely, Winnipeg and Vancouver. But the percentage increase is roughly the same. It is perhaps to be noticed that the percentage increase in the case of Vancouver is 46, and in cents per hundred pounds the increase is only 44¢ as against our 80¢ and 84¢ respectively. The percentage increase to Montreal was only 37 and your lordship will understand why it is something less than the 40% in the case of Montreal and Vancouver, the explanation being that those are competitive rates and they are increased as the railways think they should be increased. In the case of Vancouver too, they are competitive rates and they are increased as the railway thinks they should be increased. But in my submission the statement illustrates rather concretely what is happening as these rates are going. Now we are faced with another application returnable in the near future - in the next few days - for another 4.4% increase; that is on the basis of the horizontal percentage increase, the rate on the long haul, for a hundred pounds, in the case of Edmonton, is going to be twice what it is, and more than twice what it is to Vancouver.

MR. EVANS: I have no objection to the Exhibit being filed; ^{but} I just have this to say. I have not checked the rates. I do not know what my friend is proving by this Exhibit, except a mathematical truism of some kind.

THE CHAIRMAN: He is complaining about this mathematical truism.

MR. FRAWLEY: It is as to what the mathematical truism does to the long haul. That is perhaps a better way of putting it.

MR. P. C. ARMSTRONG - Recalled

EXAMINATION BY MR. SINCLAIR - Resumed:-

Q. Mr. Armstrong, immediately prior to adjournment yesterday afternoon, you had given us an illustration of pricing in a buyer's market and a seller's market. I would now ask you to apply the results as shown in your illustration to the marketing of grain.

A. The same thing happens with grain as happened in the case of my lady poultry farmer and the eggs. It is particularly apparent always in the case of grain, because the people who buy wheat in large quantities watch the wheat situation very closely. There is no commodity as to which the production, the location of supply and the market needs are more fully studied than in the case of wheat. If the freight rate on wheat or any other part of the cost of producing and distributing wheat is reduced by 1¢ a bushel, or if it is increased by 1¢ a bushel, the problem of deciding who is going to benefit or lose will be settled just as in the case of the eggs. If the market is a weak one

the buyers of wheat - importing firms in Europe or Government import boards - will know all about this. They always hear about it. So will the competent seller of wheat such as the Canadian Wheat Board. They all know what the market condition is. If the market is a weak one and transportation costs are reduced, these buyers having heard about it will reduce their offers. If they knew they could buy wheat in Canada for \$2 per bushel, with a certain rate Fort William in effect, if the freight rate goes down 5¢ a bushel they will know that they can get the same amount of wheat for \$1.95 per bushel and they will offer accordingly. If the market is a strong one, the seller knows that an increase of 5¢ a bushel will justify insistence on his part on getting 5¢ per bushel more.

Q. Can you give us a clear cut case to illustrate the point you have just made?

A. Except in the so-called Crow's Nest rates, there has been only one case of which I know in modern history in which an attempt has been made to aid the producer of primary goods for export by a deliberate and directed reduction in transportation charges. On May 29, 1929, export freight rates on wheat in the United States were reduced by amounts ranging from 6¢ per hundred pounds to Chicago from points west of the Missouri River to as high as 11½¢ per hundred pounds to New Orleans from the Missouri River.

Q. Was that a voluntary reduction or was it directed?

A. That reduction is reported by Commissioner

Mayer.

THE CHAIRMAN: Can you give us the figures again before we go on?

MR. SINCLAIR: There was a reduction of 6¢ a hundred to Chicago from points west of the Missouri River and 11½¢ to New Orleans from the Missouri River

THE CHAIRMAN: That was to encourage exportation?

MR. SINCLAIR: It was to assist in the exportation of wheat from the United States. That was the purpose.

THE CHAIRMAN: Then there is a bonus of 48¢ or 50¢ also.

MR. SINCLAIR: This is back in 1929.

THE CHAIRMAN: I thought the witness said 1949.

THE WITNESS: No, 1929, the only time when this experiment was tried.

MR. SINCLAIR: It is an experiment.

THE CHAIRMAN: Just forget what I said. I thought you said 1949.

THE WITNESS: Commissioner Mayer of the Interstate Commerce Commission, pages 703 and 734, Volume 164, I.C.C. Report, described the situation:-

"About one year ago the carriers in a commendable effort to aid in a national program to diminish the surplus supply of wheat in this country voluntarily established emergency export rates on a basis substantially lower than any rates theretofore prescribed by us. While the results of this experiment have not been subjected to the clarifying test of examination and

cross-examination on a public record in a proceeding before us and therefore the facts are not available here, it is my understanding that the emergency export rates produced no appreciable effect in moving wheat out of the country."

THE CHAIRMAN: Q. Pardon me a moment, but how long did those reductions remain effective?

A. I think the history will be worked out in detail here, sir, so that you will be able to follow the course of events.

MR. SINCLAIR: I will see that we give that point, my lord.

Q. You were going to tell us, Mr. Armstrong about when these reductions were announced.

A. Those reductions were announced on the afternoon of May 29. I remember the incident very clearly. May 30 was of course Decoration Day and the Chicago Board of Trade was closed. When it opened on May 31 the Chicago cash price - these figures are taken from the official statistics of the Chicago Board of Trade Volume for 1929 - was 98¢. For several weeks before this the Chicago cash price had been ranging from \$1.05 to \$1.07 for No. 2 yellow hard. When the market opened on the morning of May 31, the cash price for this grade was 98¢, a fall of from $7\frac{1}{2}$ ¢ to $9\frac{1}{2}$ ¢ per bushel.

Q. That is on cash grain?

A. Yes.

Q. What about futures?

A. A similar but not quite as great loss was experienced in the futures market where, of course, many

other conditions affect the price as well as such an immediate question^{as that}/of transportation costs.

Q. The Chairman asked a question, and I think perhaps it should be dealt with now. He asked how long these emergency reductions in the transportation cost of export wheat remained in effect.

A. For a while there was a general rise in wheat markets going on all over the world, in Chicago and elsewhere, and by the middle of July, 1929, the cash price had risen from this 98¢ level to \$1.45½. Then, as those of us who were familiar with grain markets at that time will clearly remember, weakness of the whole market set in and the price fell almost steadily to the low levels which prevailed in 1930. That is, the experiment to help the wheat market by freight reductions failed, since the effect was inconsiderable compared with other market factors, and the emergency rate reduction was taken out as of October 1, 1929.

Q. After those reductions were taken out, was there any effect on the cash price of grain?

A. During the two days following the removal of the emergency decrease in rates, the Chicago cash prices rose by 3¢ to 8¢ per bushel, despite the fact that this was in a generally declining market and that after the stimulus given by this increase in freight rates had been removed, prices commenced to decline again and went down steadily to the famous panic level.

Q. Would it be your view that the taking out of this emergency reduction in rates would be known to buyers?

A. They were known certainly before the market

opened the next morning. I may quote a little incident in connection with this matter. On the afternoon of May 29, 1929, when this rate reduction was announced in the press, I at once noted it in the afternoon news paper and I at once sat down and wrote a memorandum to the then Vice President of Traffic of the Canadian Pacific Railway, pointing out to him that it was inevitable ^{that} the next morning/the Chicago market would open lower by almost the amount of the rate reduction. So it was quite possible to foresee the inevitable logic of events.

Q. You are speaking of an open market under that situation.

THE CHAIRMAN: Pardon me a moment. Are you saying, then, that those who reduced the rates did not foresee this inevitable result which you have spoken about?

A. I am afraid they did not. I might perhaps be permitted to quote again from Commissioner Mayer in the same reference.

MR. SINCLAIR: That is the Interstate Commerce Commission?

A. Yes; the same reference which was given earlier:-

"The effort made by the carriers last year to reduce the surplus grain by putting into effect emergency export rates offers no acceptable test of the effectiveness of export rates as part of the rate structure. These emergency rates were put into effect late, and under conditions

such as world wide publicity which were not favourable."

I think it was exactly at that point^{at}/which they fell down; that is the point on which all those advocates of helping the farmer by reducing his transportation costs fell down. They seemed to forget that everyone from the village storekeeper to the cereal import buyer of Great Britain knows that those reductions have been made; every buyer knows that; and that was what they omitted to consider in this case. You must remember that this particular reduction was put in voluntarily by the railways and it was announced in the press at that time. I am sorry I could not go back and find the reference now, but it was announced in the press at that time that it was put in at the request of President Hoover who I do not believe was a specialist in grain marketing and who might have been thinking of trying to help the farmers, without working his thoughts out to their logical conclusion.

Q. In other words he thought that by reducing the freight rate on grain to the seaboard, he would increase the price to the farmer?

A. Either that or increase the export volume. He discovered that neither of those results followed.

Q. That is in the condition of an open market, as I said. What about a market when there is one bargain between government agencies; for example, the Government of Canada and the Government of Great Britain? Would the effect be the same?

A. The effect is not quite so immediate, naturally. There is still a free market, we must remember, in one

sense in wheat, despite all international agreements. For example, the price at which Canadian wheat is sold to Britain is not a permanent price; it is negotiated from time to time. If the world supply of wheat is very tight at the moment when a bargain is made, the Canadian Wheat Board or the official representatives of Canada will be in a position to get a price which will include any increase in freight rates within reason. If the market is a soft one, then the cereal import board in Britain, if it knows that freight rates in Canada have been reduced or are not going to be increased, will use that knowledge as a very powerful lever in bargaining. That will be one of the factors which will establish the price that they will pay at Fort William or Vancouver. But in the end you must remember that government agencies trading in wheat are still trading. They may be government agencies and think themselves perhaps above such a vulgar phrase as "trade", but they are still trading. They are trying to bargain and sell. It is still higgling in the market that is going on with, as between them the usual essential sellers resistance, in this case on collective sales. That is shown here in the fact that the Canadian Government naturally wants to get as good a price as possible for its citizens.

(Page 18060 follows)

On the other hand, there is the usual buyer's resistance. In such cases it will be demonstrated by the British Government, for example, trying to buy wheat as cheaply as possible for its citizens. The manner of trading is different; the timing of it is different. Instead of trading every few seconds on the floor of the Winnipeg Grain Exchange, you now trade in conference rooms every year or two, but you are still trading, and the rules which apply in the so-called free market will still apply under bulk trading between governments.

Q. Would you say, Mr. Armstrong, that an increase in the freight rate on grain to Fort William would lower the price to the western farmer?

MR MACPHERSON: What was that question?

MR SINCLAIR: I asked him if he would say that an increase on the rate on grain to Fort William would lower the price to the western farmer.

THE WITNESS: No. If we were still selling grain as we used to sell grain at one time, on a grain exchange at Winnipeg, or even on a grain exchange at Liverpool for that matter, if that were the condition, then I would say that a reasonable increase in the export rates on wheat would not necessarily lower the price to the western farmer; in fact, I should expect it in present circumstances not to lower that price, because in a buyer's market the price has already been pushed down to a point at which the farmers will take no less, so that in order to insure themselves of a supply the buyers would be willing to accept the increase in freight rates as a part of their cost, while in a strong market the buyers would have to concede a price increase which would probably outweigh any increase in freight rates.

Now, it should be very clear that if at this

minute you increased the freight rates on wheat to Fort William and Vancouver it would be equivalent to a reduction of the price received by the farmers in Western Canada at this minute, and as long as a fixed price lasts---

Q. You mean until further negotiation of a bulk contract is made?

A. Exactly. When the next bulk sale comes up, then the principles which I have laid down will apply, and, given adequate intelligence and energy on the part of the sellers and the buyers, given a matching of wits which is successful for both producing a fair bargain, it will be just as possible for any government agency selling Canadian wheat to get a fair return to the railway companies for carrying it as to get a fair return to the farmer for growing it.

Q. Now, Mr. Armstrong, would you think that unduly low transportation costs on grain would keep sub-marginal producers active in the growing of grain?

A. You have opened a whole Pandora's box of troubles here. Yes; yes. A subsidy of any kind to production tends to keep marginal producers in production.

Q. So that if the Crows Nest rates are lower than they should be it would have some effect on sub-marginal producers of grain in Western Canada?

A. Well, those of us -- and I think there are many here -- who know the prairie conditions well, realize of course very fully the situation. The whole economy, the whole sociology of the prairies, like every other rural area today in the world, is influenced by the presence of an unnecessarily large number of sub-marginal producers, and they can be a very serious factor in the market. On the other hand, you must remember that those of us who are shall we say sympathetic students of agrarian economics

will feel very strongly that this question of driving sub-marginal producers out is a difficult and delicate task, to be handled skilfully, you see, because you do not want to upset the sociology too rashly; but, broadly speaking, it would be to the benefit of the efficiency of wheat production, to the benefit of the efficient farmer in Western Canada over a period of years, that sub-marginal producers should not be encouraged to grow wheat by uneconomic devices such as export bounties. Of course, these rates, you understand, are an export bounty; the fact that these rates are below the normal level is an export bounty.

Q. Now would you summarize, if you can, the effect of freight rates on wheat on the income of the Canadian farmer?

A. Within broad limits, increases and decreases in wheat freight rates within Canada do not really affect the income of the Canadian farmer in a weak market, but factors leading to an increase in price are usually so much more important that a moderate increase in freight rates can be forgotten.

Q. One might wonder, Mr. Armstrong, if there would be any limit to that; would it be true, for example, that it would not matter to the western Canadian farmer whether wheat was carried free, or, on the other hand, 12¢ a bushel being increased to \$1.00 a bushel?

A. Well, the answer should be quite obvious to anyone who will think the question out. Since the average rate at present is 12¢ per bushel on wheat moving to the export outlets from the prairies, and it is therefore a very small part of the price of wheat, the effect of removing all freight rates on the prairies would simply be that in a weak market the Canadian farmer would accept 12¢

per bushel less for his wheat, if he will accept the present price -- 12¢ a bushel, the existing rate. In a strong market this country would simply be giving away 12¢ per bushel of its money, or that of some of its citizens, which it could otherwise obtain without in any way interfering with the sale of wheat.

Now, when you come to an increase of your other example, of \$1.00 per bushel, in freight rates, that might be disastrous. It would be so large in proportion to the price of wheat that the added cost imposed on even the lowest price which the farmer would accept might result in a price which would shut our wheat completely out of its markets. People in other countries might have to starve to death rather than pay these prices.

My suggestion is that no decrease in freight rates is likely to be of use to the Canadian farmer, while a moderate increase could not possibly damage his interests at any time.

Q. Therefore would you say that the unduly low Crows Nest rates were never of any use to the western grain grower?

A. Well, the former Crows Nest rates, the rates made under that---

Q. The agreement of 1897?

A. Well, yes, the non-existent agreement, the terminated agreement of 1897. The rates made under that might have been quite useful at the time. I would have been sceptical if I had been called on to advise the Canadian Government at the moment as to its policy in that respect; I would have said, Well, but you could not make any mistake. The Canadian Pacific in a moment of perhaps undue enthusiasm over the future is willing for three and a half million dollars to take the responsibility of putting these rates

into effect. I think that is ill-advised on their part probably, but as far as you are concerned you do not stand to lose anything. It is all right, nothing is going to go wrong." The market for Canadian wheat had not been established. A lower rate of that kind probably enabled the Canadian producer in those early days to horn into the market, as you may say; it gave him a chance to get into the market.

Q. What you mean is that trends, wheat trends and wheat marketing trends, had not been established -- sources of supply and one thing and another like that?

A. That was a very different world from the one in which we live at the present time or have lived for the last thirty years or so. In those days it was quite a thing to break into this new market, and I have no doubt that it was useful, I imagine, to the farmer at that time; but the condition is a very different one now, when the Canadian wheat crop is one of the major factors in establishing international wheat prices. There is no longer any case of having to horn into the market.

Q. Now, are there any authorities, economic authorities, who might support that statement?

A. Well, when you get on to economic authorities with reference to wheat marketing you get into all kinds of stories, but I mentioned just now that I regarded any concession made in respect of export rates as being the equivalent of an export bounty. Well, Ricardo says, very simply, a bounty on the exportation of corn tends to lower its price to the foreign consumer, but it has no permanent effect on the home market. Now, I must admit that that is one of those very brief economic statements to which Professor McDougall referred yesterday -- one of the reasons why economists are very sceptical about giving short

answers, because Alfred Marshall has warned us that any brief statement on economics is almost bound to be incorrect. But, despite that, I think that Ricardo has grasped the situation certainly as it existed in the England of his day, and I think his opinion is still good.

Q. You mentioned Alfred Marshall?

A. Well, this is another subject; it really bears on the whole question of wheat marketing economics. It is a very complex affair, you know. There are several factors in it which I seldom see mentioned in discussion by anyone, even by very serious students. Marshall, for example, points out that the general law of markets -- we might call it Say's law of markets or Marshall's law of markets, if you like -- has some limitations. This is a quotation:

"There are, however, some exceptions. For instance, as Sir R. Giffen has pointed out, a rise in the price of bread makes so large a drain on the resources of the poorer labouring families, and raises so much the marginal utility of money to them, that they are forced to curtail their consumption of meat and the more expensive farinaceous foods, and, bread being still the cheapest food which they can get and will take, they consume more and not less of it."

But such cases are rare. When they are met with each must be treated on its own merits.

Q. Now, you have given us two authorities.

A. I would like to back up this quotation a little bit. Giffen, I would like to point out, was probably one of the greatest authorities on the economics of grain marketing who ever lived. He was in charge of grain statistics in the British Government Service, and he was one of the founders of the Royal Economic Society, of the

Political Economy Club, and of many other quite important institutions in his time. Well, Giffen gave a lot of attention to this subject, and his opinion should carry great weight. Marshall certainly took his opinion very seriously, and I know that this is true, because here we are -- let me illustrate what happens. Do you mind, Mr. Sinclair, if I take a moment to illustrate what happens, without interrupting your questions?

Q. Go ahead.

A. Take, for example, in Italy -- personal observation will have to be my authority here -- an Italian labourer may have we will say twenty cents a day to spend on food. Now, with that twenty cents he buys a loaf of bread, a little wine, a little olive oil and a little cheese. I am speaking of the poor Italian labourer, the worker, the manual labourer. Now, suppose that the price of bread goes up to twelve cents; he has still got only this twenty cents, you see, to spend on his food. Now, he has only eight cents left to spend on the other goods, and even if the price of the other goods has not risen, that eight cents will not buy a volume of the other goods equal to what it did the day before, so his total input of food is reduced. Now, as wheat still remains, as Giffen and Marshall have pointed out, and still today remains, much the cheapest of standard foods, the natural inclination of that man will be to increase the consumption of wheat, of flour, of bread, so as to replace his reduction in the consumption of the other goods, so that actually an increase in the price of wheat there will, as Marshall and Giffen point out---

Q. Increase demand?

A. Increase the consumption, not decrease it. There is a sort of recognition of that very complex affair, and I

think this is well worth mentioning. We always have a habit of talking in this country as though the only way to sell wheat was to sell it as cheaply as possible, that if you sell it cheaply enough you will sell more. Well, that is not always the case. There come times when, as in that case, the rule is reversed. There is also the fact, you see, that we have always been up against it in Western Canada by reason of having two very varying markets. Britain, our greatest single market, has always been, as far as wheat is concerned, a free-trade market since 1846, and a market in which the one desire of the public authorities and of private merchants was to get the wheat as cheaply as possible. Now, when you went across to the Continent of Europe you found a market which was historically protectionist, particularly agrarian protectionist, and therefore it was very much contrary to public policy on the Continent of Europe to permit wheat prices to go down just in order to give the public cheap bread.

I draw your attention to a little evidence on that point which is worth remembering. The first international conference was held in 1931, and produced no special result; the second was held again in 1931, and produced no definite result; the third international wheat conference, the third of the series of international conferences, was held in London in 1933, and an agreement resulted which had in it certain provisions-- export quotas for the four chief exporting nations, an implied commitment that those nations would reduce their wheat acreage, on the false theory that there was world over-production of wheat, and the agreement broke down because the Argentine Republic would not honour the undertaking to reduce its acreage.

But the third point which is so seldom mentioned is this: There was an agreement by importing countries in

Europe to reduce tariffs and other import restrictions when the Liverpool price of imported wheat rose to 63.02 gold cents per bushel. There was a remarkable recognition, you see, of the fact that on the Continent of Europe historically -- that is, ever since Premier Maline of France, certainly since his day -- the thinking on economics in Europe has been in the direction of protection for agrarian interests, and therefore the tendency has been for them to be more ready to import wheat when the price was high, as they announced in that agreement, than to import it when the price was low. So those are a few of the special aspects of wheat marketing which I think you have to keep in mind all the time.

Q. As I understand your contention, Mr. Armstrong, it is that the price of wheat is set on an international market. The point, however, has been put forward a number of times, here and elsewhere, that the only price which matters to the western farmer is the price at Fort William, that that is all he is interested in. Now, what have you to say about that?

A. Well, the price at Fort William or Vancouver, those are prices which are functions of the international wheat market. Those are not primary markets; those are markets at which the effects of the world wheat market are reflected in local prices. The price of wheat in the world gets established like any other price, by bargaining between producers and consumers. This bargaining ends in the establishment of prices either on the floors of grain exchanges or in conferences between large buyers such as the British Cereal Import Board and the Canadian Wheat Board. The controlling market, the one which really sets all other prices, is the European, especially the British market -- the European demand interacting with the domestic supply of

Europe, plus offerings from North and South America and Australia, chiefly from North and South America, because the Australian output is apt to get into other markets than those of Europe.

(Page 18072 follows)

Now you see what happens. The first factor is the domestic production of wheat in Europe, which is colossal by any standards.

It is only as that is measured against the domestic demand in Europe that you obtain the real measure of effective demand for imports.

Europe does not live on imported wheat. Europe imports a little wheat after it has eaten its domestic crop.

That is how we arrive at wheat prices. They are arrived at on the balance between effective demand backed by the purchasing power in Europe against the domestic European supply and by offerings from north and South American supporting nations.

Q. Do these markets in Europe affect the main markets?

A. That market in turn changes the local markets in Winnipeg, Chicago, and Buenos Aires.

For convenience it has been always necessary to use some method of defining the price of wheat in Winnipeg. Usually it is the price f.o.b. Fort William which is merely a convenient definition of the price in Winnipeg. You take the price at Fort William, and that becomes the market price of wheat in Western Canada.

Q. Your view is that there is no truly separate market for grain in the sense of a domestic price and an export price?

A. There could not possibly be.

Q. And the basic factor in the price of wheat is the European demand as reflected by wheat in possession in Europe?

A. Precisely. That is a point which is too often

forgotten.

Q. And if the market in Europe is the governing factor, would it be correct to say that the cost of transportation as a factor in the price must include the cost of transportation from Fort William to Europe just as much as the cost of transportation from the farm to Fort William?

A. It must include the transportation costs from the farm all the way through to the mill in Britain, yes.

Q. So I take it from your evidence that that is a very important factor which has been underlined in considering this question of one segment of the transportation cost of wheat?

A. The total cost of transportation includes the motor movement to the country elevator.

Q. The motor movement?

A. The motor truck movement to the country elevator.

Q. Off the farm?

A. Off the farm.

Q. Via truck?

A. Yes. It is quite a factor in the total transportation cost, although we seldom or never hear it mentioned, there being no great indignation against motor truck rates.

Q. Why would you say that?

A. I have had careful studies made, and I find that it averages one half cent per bushel per mile; that is \$3.85 to Fort William, for the average bushel of wheat from the Prairies.

Q. And that would contrast with the one half cent per ton-mile that the railway hauls grain for?

A. Precisely. You must remember that is an appreciable percentage of the total cost of transportation.

Q. Who generally hauls that grain?

A. The farmers deal with each other in the matter. The farmers themselves set those freight rates.

Q. Either with their own or their neighbour's trucks?

A. That is it. The movement passes into the hands of those farmers who are particularly well equipped to handle trucking and who do it for their neighbours.

Q. You have told us the various factors in the transportation cost. First of all you spoke of the movement from the farm to the elevator; and then from the elevator to Fort William or to Vancouver?

A. By rail; and then there is the water movement from Vancouver or from Fort William.

Q. Is that part of the movement which is important?

A. That is all a part of the movement. It cannot be possible to regard it as of vital importance to the western farmer to control the rail components of this movement in Western Canada, while the large and more important water rates are not controlled. That is my reason for thinking that we lay unnecessary and ridiculous stress on the prices at Fort William.

Q. Can you tell us the proportion between the rail and the water parts of the total transportation costs?

A. The rail rates average 12 cents per bushel for an average haul of 770 miles in Western Canada.

For some time prior to the close of navigation last year on the Great Lakes and the St. Lawrence the ruling rate for cargoes, ex Fort William, transferred at some lake or river port to canal-sized ships, was, for the whole movement, 13 cents per bushel. That is, the rail

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rate from let us say Saskatchewan was four cents.

Q. Let us take Regina.

A. All right. Regina to Fort William was 12 cents.

MR. FRAWLEY: Q. I think it is 20 cents from Calgary.

A. No. Let us take the rates per bushel.

Q. I thought it was something more than that from Calgary?

A. It is not 20 cents per bushel in any case from Calgary. I think it is 15.6 cents. However, from Regina the average rate is 12 cents to Fort William.

MR. SINCLAIR: Q. Now, there is 13 cents for the lake movement.

A. For the water movement down to Montreal.

Q. What about from Montreal? Have you checked on the water movement from Montreal to Europe?

A. Yes indeed. Within the last couple of weeks the ruling ton rates on liners --

THE CHAIRMAN: Are you giving the full lake and rail?

MR. SINCLAIR: I am taking the rate to Fort William as at 12 cents, and the rate from Fort William in large grain cargo-carrying boats down to Prescott, and from Prescott to Montreal.

THE CHAIRMAN: The 13 cents which you refer to includes the rail as well as the lake?

MR. SINCLAIR: That is the total cost laid down from Regina to Montreal.

THE CHAIRMAN: We are talking of Fort William to Montreal, both the lake and the rail.

MR. SINCLAIR: Quite so.

THE WITNESS: I think there is a little confusion; that is, the normal movement of wheat, the great bulk of the movement of wheat is by all water from

Fort William to Montreal.

THE CHAIRMAN: Q. If it is all water in the proper season, it is 13 cents?

A. That is it.

Q. Then how is it that it is all rail from Fort William to Montreal?

A. It is more than that. I have not got it right here. Oh, yes, here it is; it is 40 cents all rail per 100 pounds to Montreal; 24 cents to Fort William to Montreal lake and rail.

COMMISSIONER INNIS: Q. You mean by the Georgian Bay ports?

A. By the Georgian Bay ports.

MR. SINCLAIR: Q. Having got the grain to Fort William by water and to Montreal, you are going to give the Commission the liner rates?

A. Yes.

Q. Would you distinguish here between liner and tramp?

A. Liner rates are apt to run under tramp rates because a liner has to sail on a certain date and, if it has not got enough cargo, then it must take on ballast.

Now, wheat makes a very nice ballast. So liner rates are usually bargain rates for wheat when compared to a tramp steamer which comes into a port expecting to load a cargo of wheat.

The rate from Vancouver to Europe, a couple of weeks ago, was in the neighbourhood of 56 shillings per ton of 2,240 pounds.

THE CHAIRMAN: Q. From where?

A. From Vancouver to Europe, which means about 23 cents a bushel at the present rate of exchange. On the other hand, the rate by tramp steamer from Vancouver

to Europe is about the same as the liners.

MR. SINCLAIR: Q. What about the rate from Halifax or St. John to the United Kingdom?

A. The rates from St. John or Halifax to the United Kingdom, which were the same rates prevailing from Montreal while the navigation season was on, range rigidly at 8 shillings per quarter of 480 pounds.

Q. And per bushel?

A. 15 cents per bushel at the present rate of exchange. Then you get a rate from the rate-break-point to, let us say, Wilkie, Saskatchewan, not including insurance and other factors, you get a rate which would be 35 cents via Vancouver, and 40 cents via the east, to Montreal or the Atlantic ports.

Q. The point is that you say the uncontrolled and uncontrollable water rates on export wheat from Canada considerably exceed the rail rates to Fort William?

A. Yes; and that brings up this other very interesting consideration. I wonder if the Commissioners would like to look at this map?

Q. Have you a reference to the breaking point which you mentioned?

A. Yes. This map illustrates it.

I have here a map which divides Western Canada for this purpose into regions A, B and C. It will be a foundation for a little argument which is now starting.

Region A is the region which in a freight rate sense all wheat is tributary to Fort William. That is the area in which the rate per bushel to Fort William is the lowest rate.

Area C to the west is the area which occupies the same relation to Vancouver, the area from which the rates to Vancouver are below those to Fort William.

Now, area B in the middle -- the middle area is the area in which the rates are identical to both Fort William and Vancouver. It is quite a large area. A lot of wheat comes out of that area.

MR. MacPHERSON: I wonder if the witness would mind defining the area. We do not know the boundaries of it.

MR. SINCLAIR: I think this map might well be put in as an exhibit.

THE WITNESS: I think we will have to do that.

MR. MacPHERSON: Q. Exhibit or not, I am concerned with the boundaries of C. Where does C start?

A. The map is here. It is not definite.

THE CHAIRMAN: Q. You might define it by the railway stations?

A. Yes. It could be defined by railway stations.

Q. On the different lines of railway?

A. Yes.

Q. Maybe you could indicate for us exactly where C begins?

MR. SINCLAIR: Q. Possibly the witness could describe it in general terms by looking at the map, the broad outlines of the breaking point area.

COMMISSIONER INNIS: Q. Doesn't that border change as the ocean rates change from Vancouver?

A. Oh, no, no. The rail rates are fixed.

Q. But even so?

A. I will come to that in a moment.

You see, one of the difficulties of this, Mr. MacPherson, is that it is not a rate area bounded by two straight lines. But I can tell you roughly that it embraces Western Saskatchewan and a small amount of Eastern Alberta, and that it might consist of Wilkie or Battleford. Battleford is on the east side.

THE CHAIRMAN: Q.What are you talking about?

A. This is my area B, the area in which the rates are uniform to both places.

THE CHAIRMAN: If we could have area B set out, then it would give us both area A and area C.

MR. SINCLAIR: I wonder if, with the help of our traffic officers --

THE CHAIRMAN: You could file an exhibit?

MR. SINCLAIR:Q.Yes, and we could give copies of it to our friends.

A. I think you will understand what it is when I say it is just about the same distance --

THE CHAIRMAN: Q. I understand it is on the main line of the Canadian Pacific; area B is very, very narrow.

A. We would simply have to have a map or an exhibit of some kind.

Q. The area which looks towards Vancouver begins about Maple Creek?

A. Yes, it begins about Maple Creek. The rest of Alberta is in area C.

Q. But on the main line of the Canadian Pacific, from Maple Creek on west, everything is in area C?

A. Everything is in area C. It is very narrow at that point and much wider --

MR. SINCLAIR: We will have a map prepared at the noon hour and we will give a copy of it to Mr. MacPherson.

MR. SINCLAIR: Q. What about the through rates to Europe from the breaking area; how do they compare?

A. That is exactly the point which Dr. Innis wanted to raise. Let us take Wilkie, because it happens to be in that area; I mean Wilkie, Saskatchewan.

THE CHAIRMAN: Wilkie is in the B area?

A. Yes, Wilkie is in the B area. Well, the Wilkie rate to Vancouver and the rate to Fort William are identical.

The through rate from Wilkie, at this moment, according to my latest information, as well as for some months past, the through rate from Wilkie to Europe has been, taking transportation and major transportation items only, and omitting minor details and handling charges, 35 cents a bushel, compared with a rate via Fort William of 40 cents. You may wonder who gets the 5 cents difference. I will tell you. The British Cereal Marketing Board gets it.

MR. SINCLAIR: Q. It does not go to the farmer?

A. No. The Canadian Wheat Board agreed to deliver this wheat at the same price. Therefore any savings are savings to the buyer.

Q. What about the Canadian Wheat Board? Do they not get a different price?

A. No. They sell at the same price. They sell to the British Cereal Marketing Board at a fixed price, and they pay the farmer the same price at the station, but with one very interesting exception.

At this moment the Canadian Wheat Board has a policy in effect which could not have been applied under the Winnipeg Grain Exchange system, but which, in a government monopoly can be applied, and it is a system by which the farmer west of the neutral area --

THE CHAIRMAN: Q. You mean area C?

A. I mean area C, may have his wheat transported to Fort William if the market so justifies, and the Wheat Board will pay him, not the railway. It will pay him the excess cost of moving it to Fort William instead of to Vancouver.

Mr. Frawley said the rate from Calgary was 20 cents a bushel. It is 15.6 cents a bushel to Fort William.

The rate from Vancouver to Calgary is 12.6 cents per bushel.

THE CHAIRMAN: Q. You mean twelve decimal six?

A. Yes, twelve decimal six. That means that the rail rate to Fort William is 3 cents higher than the rail rate to Vancouver.

If the Wheat Board should find, for any special reason, that it must move the wheat to Fort William, it would take a lower rate to Vancouver.

MR. SINCLAIR: Q. Why would the Wheat Board find that they had to move it to Fort William rather than to Vancouver?

A. Well, they do.

THE CHAIRMAN: Q. Would it be because of elevator space at one or the other?

A. It could be, but that is not the usual condition; it is rather the tonnage available for shipping. That is the big point and the controlling factor.

Q. You mean elevator and available tonnage and storage?

A. Elevator and available tonnage and storage and the supply of wheat available. Oh, there are all sorts of special complications which come in.

From August 1, 1949, to March 13, of this year, 13,220 cars of wheat were loaded in Alberta. Therefore practically all in that area C, 13,220 cars of wheat were loaded in Alberta for furtherance to Vancouver; and 4,457 went eastbound.

When we ask: Why did this particular thing happen this year, they say: The particular reason this year is that there is quite a bit of low grade wheat in

1. The first part of the document discusses the importance of maintaining accurate records of all transactions and activities. It emphasizes the need for transparency and accountability in financial reporting.

2. The second part of the document outlines the various methods and techniques used to collect and analyze data. It includes a detailed description of the experimental procedures and the statistical analysis performed.

3. The third part of the document presents the results of the study. It includes a series of tables and graphs that illustrate the findings of the research. The data shows a clear trend of increasing activity over time.

4. The fourth part of the document discusses the implications of the findings. It suggests that the results have significant implications for the field of study and may lead to further research in this area.

5. The fifth part of the document concludes the study. It summarizes the main findings and provides a final statement on the importance of the research.

that area, and you cannot sell low grade wheat in Vancouver as easily as you can sell it by moving it east. So this gets tied up, even with the fact which the Board of

Transport Commissioners has seemed to neglect, that there are some mountains between Alberta and Vancouver.

I shall now quote the Right Hon. Mr. Howe from page 807 of Hansard of this year.

He had been challenged by some wicked person -- I suppose an opposition member, to say why it was that our exports to Britain were going down. Mr. Howe didn't seem to feel that the exports were going down unreasonably, so he said:

"My hon. friend knows the reason. He knows that the railroads in British Columbia which carry our exports to seaboard in the winter months were blocked."

So actually there would be no doubt at all that the movement of wheat this year has been influenced and that more has moved east than west because of the unusual winter in those non-existent mountains.

And then, on top of that, I would be willing to argue that it has been a definite factor by reason of the ocean rates and the two routes.

THE CHAIRMAN: Q. Did you not mention something about compensation being made to the shipper by the government?

A. Yes. The government, I believe, out of the total fund of the Canadian Wheat Board -- oh, I am sorry. I must alter that. I should say out of the fund of the Agricultural Prices Support Board. That is right.

Q. What happens?

A. The government takes the money so that the man in Calgary, whose wheat goes to Fort William instead of to Vancouver, does not lose the three cents extra which

CHAPTER I. THE DISCOVERY OF AMERICA. The first discovery of America was made by Christopher Columbus in 1492. He sailed from Spain in search of a westward route to the Indies, and after a long and perilous voyage, he landed on the island of San Salvador in the West Indies.

His discovery opened up a new world of trade and commerce for Europe. The Spanish government, under the leadership of Isabella and Ferdinand, claimed the newly discovered lands for Spain, and Columbus was appointed governor of the Indies.

Columbus's voyages led to the establishment of Spanish colonies in the Americas. The Spanish government sent expeditions to explore and settle the new lands, and the discovery of gold and other precious metals attracted many settlers.

The Spanish colonies were governed by the Spanish government, and the settlers were required to follow Spanish laws and customs. The Spanish government also sent missionaries to convert the native population to Christianity.

The Spanish colonies were a source of wealth for Spain, and the Spanish government used the wealth to strengthen its power in Europe. The Spanish colonies also played a role in the development of the Americas.

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it costs to move it to Fort William.

Q. It is refunded to him?

A. Yes, it is refunded to him through the Wheat Board but not through the railway.

COMMISSIONER INNIS: Q. I think that border which is set up on the map is not accurate.

A. No. It shows an unrealistic situation in which we find ourselves when we control one little factor of the total transportation charges, the rail rates.

The rail rates mean that there is this border, as far as the railways are concerned. But as far as the through rates are concerned, the border is shifting backwards and forwards, if you include ocean rates.

MR. SINCLAIR: Q. You think that even if there was a difference in the cost of moving the grain to market, depending whether it went ex Vancouver or ex the lakes, that the farmer would not get that advantage of the saving by moving on account of the competitive situation?

A. No. And he never did.

Q. Would that be true of the open market?

A. Yes. That was true of the open market.

I have seen fellows on the docks at Liverpool getting it. There is a lot of misunderstanding about wheat marketing.

Here in Canada we have a beautiful and fine system of elevators, storage, controlled rates, grading and inspection; and everybody in this country seems to think that you will find the same sort of thing operating on the docks at Liverpool.

But there is nothing of the kind in England. There you may have a couple of cargoes of wheat of exactly the same grade which will sell at different prices just because one buyer happens to be a little easier or a little

harder than the other.

The International Wheat Board market is not like the Canadian wheat market.

Q. You mentioned these differing competitive conditions such as the tonnage of wheat available in different positions and the tonnage of shipping. You might explain that a little more fully.

A. Well, you start out, as the Chairman observed, with elevator space.

Suppose you cannot handle the wheat through Vancouver any faster than the elevator space permits. Now, elevator space obviously is not the primary condition because there is a perfectly good elevator at Prince Rupert, yet mighty little wheat goes through there.

Q. Simply by building an elevator you cannot make a place a grain shipping port?

A. No. And what makes it one is the willingness of ships to go in there to get the grain.

Q. And the willingness of buyers to bid for cargo space to haul that grain?

A. Yes. And what effects the willingness of the ship operators is:

No. 1 - That they can enter with a cargo, and they will want a cargo to take out. They find that preferable to going around in ballast to another port. That is one reason, namely, that shippers are available for wheat.

No. 2 - Another reason is that you may be in an area in which there is a lot of shipping movement going on to different ports, and where it is a relatively small thing to move a ship empty in ballast from the point where it unloaded its cargo to another port to pick up another cargo.

These conditions differ in different parts of the country and at different times.

Vancouver is quite an important port. But on the other hand, Vancouver is always at some disadvantage when compared with eastern ports, because the North Pacific is not so full of all kinds of shipping as the North Atlantic is, so that you are not as likely to have as many ships coming into Vancouver in ballast looking for a cargo as you are in the case of eastern ports.

That is one of the reasons. But there are all kinds of reasons. I can only give you a few samples. That is all.

Q. Is this a possibility: That by maintaining unduly low rates on the rail transportation of grain in Western Canada, it does not result in higher prices to the western farmer, but rather it enables the water carriers to exploit the situation?

(Page 18093 follows)

A. They have been very good from time to time. There has been quite a notable affair from time to time, that the shippers would cash on very nicely.

Q. So that there is a possibility that this unduly low rate on grain has been softened off to the advantage of a tramp steamer operator or a liner operator on the Pacific, through the Panama Canal and around the Atlantic?

A. Oh, yes. I would like to make it perfectly clear. I am not charging that any particular person except the farmer gets the money that the farmer has been inclined to think that he was saying by low transportation charges. That may go to the farmer in rare cases; it may go to the dealer in grain anywhere on the way -- the many hands through which the grain passes; it may go to the ship owner, to the inland ship owner, it may go to all kinds of people, all sorts of people may get it, but I am pretty sure everybody else is going to have a cut at it before the farmer gets any of it.

Q. Now, the argument has been put forward that the Western Canada farmer, situated farther from the sea than any other group of important wheat growers, is in particular need of low freight rates; what do you say as to that?

A. Well, it is quite true that the rail haul of wheat from Western Canada is longer than that on wheat from any other important area except the Western United States. However, as far as the cost of transportation affects the price of wheat, it has to be the total cost of transportation, not only the cost of the rail part of the journey. Certainly the Western Canadian farmers are not at a disadvantage owing to high rail rates, never mind what their disadvantage is as to distance. The average rate on wheat from western farms to water is 12¢ per bushel for an average haul of 770 miles. For a similar haul in the United

States the average rate -- I propose to offer special evidence on this point, but I should like to mention it at the moment -- the average rate is certainly more than twice that. A typical rate in the Argentine Republic is 19.3¢ per bushel for 186 miles.

THE CHAIRMAN: Q. Is that the longest haul there is in the Argentine?

A. Well, it is one of the longest hauls, sir, because Argentine wheat very largely moves from inland points to rivers, you see, on its way out. In the State of Victoria, Australia, there is an average rate of 6.76¢ per bushel for an average haul of 180 miles. I made attempts to obtain other rates from other countries, and we have had the greatest difficulty in doing it, but those are bona fide figures which we obtained from accredited sources. So as far as transportation is a factor in wheat prices at all, the Canadian farmer is certainly at no disadvantage. He is the best situated in the world to the extent to which that helps him. The present situation in which the farmers of the Western United States are getting more for their wheat on the farm than Western Canadian farmers, although freight rates in the United States are at least twice as high as in Canada, would certainly go to indicate that rail rates are not the major item in fixing the price which the farmer gets for his wheat; they are an insignificant part of it.

MR SINCLAIR: Q. In view of your evidence, Mr. Armstrong, and your knowledge of Western Canada, how do you explain the very deep-rooted belief among Western Canadian farmers that the maintenance of the Crows Nest rates is the one great matter of importance to them?

A. Well, you know, it is a tradition; it is almost a superstition. It is not the result of serious study of the

problem. Everybody has been told that by his father and his uncle, and he goes on being told that, and he tells his son that -- "Look at the Crows Nest rates; these wicked fellows are going to take them away from us." But it is a superstition, you see. Western farmers hear the price of their wheat quoted at so many cents per bushel at Fort William. Everybody in Western Canada knows that. He knows the price at Fort William is so much, and---

Q. He gets it over the radio every day?

A. Exactly, all the time. Now, he knows that at a certain point in Western Canada he will pay so many cents per bushel for rail rates to Fort William, so he knows positively that he gets the Fort William price that day less the rail rate to Fort William, and you can't convince him that he doesn't, because he knows he does, and he knows that Farmer Jones a little farther down the line pays more, or Farmer Tompkins in the other direction pays less. So he comes to the single conclusion that all the world depends on the Fort William price less the rail rates, you see. Now, that is a very natural way to feel. Then you must remember that this situation, this story, has offered blessed opportunities, you know, for people who, for good or bad reasons, would like to be popular with the western farmers. It is a wonderful story to tell. I have never attempted to run for Parliament, but I cannot imagine a better platform on which to run in Western Canada than to show the western farmer that the Crows Nest rates are the palladium, the shield, which stands between him and disaster. Mind you, I am not charging people with deliberate mis-statements.

MR MACPHERSON: I do not think, Mr. Chairman, there is any suggestion of even insinuating it, because the fact is true in Western Canada, certainly in my province, that,

irrespective of any man's political belief, he has the deep-rooted view as to Crows Nest rates, and does not regard it as a superstition; and I want to say that we do not even appreciate the insinuation that there is something ulterior or sinister in the attitude that is adopted.

MR SINCLAIR: I think, Mr. Chairman, that Mr. MacPherson, if he will just wait a little while, will see---

MR MACPHERSON: I have waited long enough.

MR SINCLAIR: Now, just a minute, Mr. MacPherson. If he will just wait a little while he will see that our evidence here is being advanced to show that, irrespective of what they may believe, the facts are that it does not happen the way they think it does. Now, whether that is a result of father telling son, or whether it is a result of Mr. MacPherson telling him, makes no difference.

MR MACPHERSON: My objection---

THE CHAIRMAN: Mr. MacPherson, the witness maybe is a bit lurid in his description of this case, but he is giving it. You will have every opportunity that you desire to cross-examine upon it.

MR MACPHERSON: I realize that, but I wish to register my objection to the suggestion that people were deliberately supporting this as charlatans in our country, which is not true.

MR SINCLAIR: There was no suggestion of that.

THE CHAIRMAN: You will have, I think, a more effective opportunity in a little while.

MR SINCLAIR: Q. Now, Mr. Armstrong, from what Mr. MacPherson has said, you see the situation, and, assuming what you say is right, the farmers may still be convinced that you are wrong, and I think that you will admit that it is going to take us a long time to persuade them to any different view. Now, under those circumstances

-- and I think they have been pointed out very adequately just now -- you must, I suppose, have some situation in mind or some proposal to deal with the situation?

A. You see, that is a very difficult question, it comes so close to discussing political methods in a democracy, because there is nothing improper in a man offering the western farmer the argument that the Crows Nest rates are important if he believes it. There is no good reason why he should not. I think it makes an excellent argument to offer, if you believe it, as Mr. MacPherson does. So I am not suggesting that I should be asked to explain how I am going to cure the farmers. If Mr. MacPherson and myself agreed about this and we stumped Saskatchewan together, we might change their minds, but that is going to be difficult, so what we have to do is to get down to realistically considering what are the difficulties of the western farmer and what we can do about it. I say certainly not freight rates. Now, what are his difficulties? Has he got difficulties? What can we do about it? The farmers of Western Canada know -- they are not fools -- they know what happens to them when the price of wheat goes to disastrously low levels. Some of us in this room must have been on the prairies during the great drought and depression, and anyone who was on the prairies in those years and did not realize that the Western Canadian farmer was suffering, why, he must have been blind. There were such people, blind people, but they could not see that the western farmer was suffering. There is a thing that we have to face; the western farmer went through this. Now, what are we going to do about it? Too few of the other people of Canada fully realize the conditions there, nor do they realize to what extent the disastrously low levels for wheat on the prairies were reflected in unemployment, bankruptcy and distress of all

sorts of other Canadians in different parts of the country. I saw men by the hundred on the street in Montreal because of the drought and depression on the prairies.

Now, the answer is that the most profound believer in the over-all wisdom of maintaining free markets and letting prices rule the economy is bound to see that this is one place where there is a higher law than any law of economics, and we cannot ever permit a recurrence of a disaster of that nature. Even the most profound believer in freedom of markets has to see that western farmers still have to sell their wheat in the world market, in which they can be accorded no sort of protection by the government of their nation, while, broadly speaking, the rest of the economy of Canada has been sheltered to no small extent by tariffs. Now, I am not going to get into the argument as to whether tariffs are right or wrong; there is a fact. The Canadian economy---

MR FRAWLEY: That was not in your notes, I suppose.

MR SINCLAIR: There are a lot of things not in my notes, Mr. Frawley.

THE WITNESS: Might I make a short statement at that point, Mr. Chairman? Mr. Frawley has now suggested that we are dealing with notes that are prepared. Yes, these notes have been prepared, by me. These are my opinions as asked for by my client, the Canadian Pacific Railway. I prepared them, and I am adding to them any other opinions that occur to me as being interesting for the Commission. This is not something that somebody has given me to read. It is not a brief in any sense.

MR FRAWLEY: Mr. Sinclair did not give you all those notes; I am sure of that.

MR SINCLAIR: Not at all.

MR FRAWLEY: I am sure of that.

THE WITNESS: The Canadian economy is so geared to the production and sale of wheat that it has been quite impossible at any time to make the suggestion that the only thing to do is to let the sub-marginal fellows be pushed out at the bottom till the production of wheat is reduced by sheer hard times. That would be a disaster to this nation and to the world. The world is largely dependent on the supply of Canadian wheat, and the Canadian economy certainly is dependent on its production and transportation, and it must be kept going if we can possibly do so, for the most overwhelming reasons. So, however much anyone may detest the idea of subsidies, there is a practical and overmastering necessity to use subsidies of some sort if and when the time comes at which Canadian farmers face a price disaster. The important point that I am trying to rub in is that the idea of subsidizing western farmers in respect of wheat production by forcing Canadian railways to carry wheat at abnormally low levels is a poor one. It is the poorest form of subsidy of which I can conceive. It is difficult for me to imagine a less effective form of subsidy, a less certain method of protecting western farmers against disaster.

THE CHAIRMAN: Q. Are you not saying throughout that it is not a subsidy at all, because they do not get any benefit from it?

A. That is exactly why I say it is the worst kind of subsidy. It is an attempt to subsidize him, but it is ineffective, sir; it does not produce the results which are hoped for.

THE CHAIRMAN: Well, we will adjourn for a few minutes.

(Recess)

(Page 18101 follows)

---On resuming:

MR. SINCLAIR: Q. Before recess, Mr. Armstrong, you had been discussing the depressed conditions in Western Canada arising from droughts and world-wide depression, and the fact that the farmers must have some protection from those conditions, if they ever do return, and you were pointing out that/^{the} use of one factor in the transportation cost was a very poor way to help the western farmer. I would now ask you to give the Commission your suggestion as an alternative to that undue low rate as one factor of the transportation cost?

A. I am afraid, Mr. Sinclair, that my own suggestion is that we must get on with the enormous task of convincing the people of modern nations that they have been neglecting their agriculture to a dangerous extent and that there must be a fair deal for the farmer all around.

Now, there are two specific methods which might be applied at the present moment and about which there is much argument. One method is to prevent another price disaster by international sales agreements. That experiment may succeed or it may fail. If this be the correct way of handling the situation then the protection is obtained by the Canadian government selling Canadian wheat at a price which will enable the Canadian farmer to obtain a reasonable return for his wheat after paying normal costs of production including the normal transportation charges.

Q. That is, in those cases where the transportation charge is paid by the farmer that must be a factor which the government should take into account in fixing the price of wheat.

A. Certainly. If, on the other hand, this method

should not prove satisfactory, then in the more or less experimental stage the alternative would be of course to permit Canadian wheat to be sold in an open market with protection against a price disaster by the national government guaranteeing a floor price ^{to the farmer} /below which the price of wheat would not be permitted to go.

Q. Those are two possible methods. Have you in mind any other?

A. No, I don't know any other method. In neither of these methods does it appear that there is any useful part played by the establishment of an abnormally low rate for rail transportation of wheat in Western Canada. The problem is far too great to be dealt with by such a clumsy expedient by seeing that Canadian farmers can ship wheat for a few cents less than is reasonable. Remember that incidentally these Canadian farmers share with all the rest of the Canadian people in having to provide the railway companies with higher rates on other products with the result . . .

Q. That is proportionately?

A. Yes. ^{Q.} / The amount by which wheat rates are not remunerative must be transferred to them through higher rates on other commodities that are inbound or outbound?

A. To them and the rest of the Canadian people as Canadian citizens. There is no use in arguing that Canadian farmers should be able to ship wheat for a few cents below the normal rate and pay higher rates on other products.

High rates on wheat are not convenient or practicable. The proportion of the problem should be kept in mind. What this nation has to be protected against is the condition in which wheat will sell at

thirty, forty cents a bushel, -- that is what we must protect the nation against. Not only the farmer, the nation has to be protected against that, so that the needed protection, as it would have had to be applied during the great depression, is a matter up to a dollar a bushel or more.

THE CHAIRMAN: How can you protect the nation; the nation cannot protect itself?

A. What I am trying to say is this, that a price disaster to the farmer is a national disaster involving all of us, it involves every citizen of Canada sooner or later and for that reason I say we must protect the farmer as a part of a necessary national policy.

MR. SINCLAIR: And that is why if there is a free market there has to be a guaranteed floor?

A. Yes. Now, remember I do not like guaranteed floor prices, I do not like subsidies, I am a believer in a free market economy; but I draw to your attention once again that the western farmer has to sell his wheat in an unprotected market in the world while he lives in what is very largely a protected economy, and so important is his problem to all of us that in no circumstances can we allow doctrinaire devotion to freedom of the market to incline us to refuse even unorthodox measures to protect the Western farmer.

THE CHAIRMAN: Are you quite right in saying he is selling in an unprotected market in the world? Did you not point out that the nations of the continent did protect the market, and very safely, too.

A. Yes, but he is selling in a market in which the Canadian government, his government, cannot control the prices to him.

THE CHAIRMAN: But he is selling in that market.

A. That does not do him any good. It may protect the farmer in Germany, for instance, but it makes it more difficult for the Canadian farmer.

THE CHAIRMAN: But the point is he did sell it in a protected market,

A. He did but he did not get as much for it as if he had a free market in Germany.

THE CHAIRMAN: ^{Q.} He sold it in Britain too? fifty million bushels of it?

A. Yes, that is a free market.

THE CHAIRMAN: ^{Q.} He sold in those same years about fifteen million bushels in Belgium?

A. Yes, in a protected market. I think it was more than fifty million bushels in Britain, it is consumed in Britain, they are now buying 140 million bushels a year. Even in those days we sold in Britain 150 million to 250 million bushels a year for British consumption.

THE CHAIRMAN: What I am a bit worried about now is how far we are going in this, this is getting into an inquiry on wheat.

What is the case you want Mr. Armstrong to make, Mr. Sinclair?

THE WITNESS: This is in support of the Canadian Pacific contention that the Crow's Nest rates can be freed from statutory control without involving a disaster to Western farmers.

MR. SINCLAIR: A number of briefs have been filed -- by the U.G.G. the Western provinces and so on -- and I will ask Mr. Armstrong shortly, after I have laid this basic material, to direct his attention to some of

the statements that have been made in these briefs and which have been put forward as views to this Commission as to why rates on grain should be fixed by statute and why they have to be kept low.

Q. Now, would you, Mr. Armstrong, summarize your views that you have been giving us during the last few minutes?

A. Abnormally low freight rates on wheat are a clumsy, inadequate, ineffective method of giving assistance to wheat growers in Western Canada. It is uncertain and most improbable that any reasonable increase in these rates would actually be paid by the farmers. Any alterations in rates charged on export wheat from Canada are far more likely to be absorbed by ocean carriers than to affect the pocketbooks of western grain growers. If protection for the western farmer against price disaster is required, it should not be, in my opinion, in this direction.

Q. Now, Mr. Armstrong, in view of the fact that we have these submissions from a number of western provinces and organizations, I would ask you to direct your attention to them, and first, to that brief which has been filed on behalf of the three prairie provinces of Alberta, Saskatchewan and Manitoba.

Q.
COMMISSIONER INNIS:/ Are you in favour of subsidies but not subsidies paid to the railways?

A. I say that in an emergency, a wheat emergency such as we have had in the past, there have to be subsidies but not through railways. After all, there are three ways in which a western farmer can be poor: a western farmer can be poor because of incompetence, lack of thrift, wastefulness -- like any of the rest of us --

in such a case we cannot do much for him, I am afraid; the western farmer can be poor -- might I, to save the feelings of my friends from the West say that this is more infrequent among western farmers than in any other part of Canada, they are all the best citizens -- as I was saying there is the second form of poverty which may arise from drought. Now, that is obvious. You cannot take care of that at all by giving a subsidy on production either directly or indirectly through freight rates, even if I am wrong and the freight rate subsidy would help the farmer.

So you come now to the third and major question, in my opinion, and that is the broad question of how to see that the western farmer gets an income, overall, proportionate to his activities as compared with the rest of the community. Now, that is as I say, a secular problem, it is a world-wide problem.

COMMISSIONER INNIS: That is very much your position as you put it before, Mr. Evans?

MR. EVANS: Oh, yes.

THE WITNESS: That is the point. I do not think it is much good trying to give it time in this specific way which won't work, particularly if the man who is hard up because of drought and which, in any case, is so inadequate -- what can you do with a few cents a bushel when the problem is one you measure in dollars a bushel between success and failure?

MR. SINCLAIR: Q. You mean thirty, forty, and fifty cents as compared to a dollar a bushel?

A. Yes.

Q. Turning your attention to the brief of the prairie provinces on grain, do you think the present system of rates on grain corresponds with that which

the agreement of 1897 was intended to bring into effect?

A. Fortunately, there is complete agreement between the brief and myself on this point because the brief denies that. It points out that the original rates as provided by the former Crow's Nest Agreement applied only to points on the lines of the Canadian Pacific Railway which were in existence at the time when that former agreement was signed. The amendment to the Railway Act of 1925, of course, terminated the agreement in my opinion, extended the grain and flour rates established under the agreement to all railway lines in Western Canada, and then on top of that --

Q. And to all shipping points?^{A.} Yes, and on all lines of railways, Canadian National, Canadian Pacific, Canadian Pacific/^{lines}built after 1897 as well as those built prior to 1897. Now, on top of that in 1927 by general order 448,^{of} the Board of Railway Commissioners, it was directed that the rate should also be applied to grain moving to Pacific ocean ports for export, although the former Crow's Nest Agreement which was terminated at that time, in 1925, covered only grain and flour eastbound to the head of the lakes.

Q. You have stated that the brief is in agreement with your statement on that point, and it is admitted in the first paragraph of the brief, where I read:

"Though their field of application has been expanded by legislative action in certain directions it has been restricted in others, with little possibility that the balance of advantage or disadvantage from such adjustments can be appraised with any degree of accuracy."

Have you any comment on that?

A. This is a correct statement of the economic consequences of the public policies which have been followed in this case. It is a correct description of the situation. As the brief points out, the Crow's Nest Pass Agreement was suspended, I think, in 1918.

Q. That is correct.

A. It was suspended in 1918 and it was never brought back even into theoretical effect. It was replaced by an entirely new system of rate regulation having no relation to the former Crow's Nest Agreement. So I say that economically speaking, the Agreement as made originally does not establish rates on grain and flour in Western Canada from points on lines which were not in existence at that time. I think it is a very mistaken picture to say, as the brief does say, that they were established by a voluntary agreement between freely contracting parties.

Q. Now, Mr. Armstrong, have you any further comments on the economic arguments set forth in the brief of the prairie provinces?

A. Yes, on pages 5 and 6 of the brief, the argument is built up that prior to the former Crow's Nest Agreement, construction of the Canadian Pacific did not provide the West with adequate opportunity for agricultural expansion because rates were not controlled. It was argued that the agreement had to be entered into in 1897 to correct the situation. That statement contrasts with the statement later in the brief intended to prove that the rates under this agreement were never of economic effect.

Q. Any further comment on the brief?

A. Yes. It surprisingly to me makes no attempt

to establish economic value of the so-called Crow's Nest rates. On page 20 the statement is made that the Crow's Nest grain rates represent established national policy, the alteration of which would be ruinous to the wheat-growing areas.

Q. That is a quotation of the first sentence on page 20 of the brief.

A. That is an economic doctrine which I find it difficult to accept. It has also been pointed out that rail transportation charges averaging twelve cents per bushel on wheat can scarcely be a major factor in deciding the economic fate of Western Canada.

THE CHAIRMAN: Q. If you increased that charge to twenty cents a bushel, it would not make any difference?

A. It certainly would not decide the economic fate of Western Canada.

Q. That is not the point at all.

A. That is what they are saying.

Q. I am just wanting to know what you are hinting at. I think if I have understood you so far it really does not matter what freight rates are paid in Western Canada, that the world market absorbs them anyhow.

A. Within reasonable limits, I would say the weight of evidence is all in that direction, to the extent you do increase rates in Western Canada, you are not going to hurt the western farmer at all.

Q. Can you tell us what a reasonable limit would be? You have given us a figure of twelve cents per bushel. What would be a reasonable extension of that figure without making any difference in the return to the western producer?

A. That is, sir, a matter that would have to be

set by market conditions, but I can only say this,

that any new rate on grain which replaced the so-called Crow's Nest rates would have to be worked out by the railways, the interests affected and the Board of Transport Commissioners.

Q. It must be, then, a delicate subject to interfere with?

A. It would be a problem to be dealt with very carefully because anything which affects a large industry must be dealt with very carefully. But I would say this, according to ^{Mr.} MacPherson's calculation, it would be only reasonable to double these rates, it is not a wild one. The outlook as I see it at the present time, I am not alarmed over that. I say the thing will have to be studied carefully and I hope almost prayerfully by the Board of Transport Commissioners, the railways, and by the interests concerned, with the one object of getting fair treatment for the railways without endangering the interests of the farmers of Western Canada.

Q. Then you cannot dismiss the desire of the western farmer to keep those rates as they are. Just offhand you admit it is something that may have an effect on his price?

A. It may. You see, I am very doubtful.

Q. How would you fix any rate unless you have a lot of people with competent knowledge to consider it all very carefully. Therefore, you must admit there is a question.

A. Suppose you said to the railway companies 'Now, we have repealed the statute and you fellows go out and get what rate you can on your wheat', well, suppose, in a moment of lunacy, speaking in terms of the present conditions, we said, 'All right it is dollar a bushel,

the average rate in Western Canada.' Well, there could be no doubt to any reasonable man that such an increase in rates would unfavourably affect our policy to sell Canadian wheat abroad at prices where they are. On the other hand, with world prices where they are, I would say quite a substantial increase could be given at the present time without any danger of upsetting the apple-cart.

(Page 18117 follows)

MR. SINCLAIR: By that you mean passed on?

THE CHAIRMAN: Q. You would not say how substantial?

A. I think that is a matter which would require most careful consideration. I must be very careful.

Q. Might not such consideration show that the rates should be even more?

A. That is extremely improbable, in my opinion. And we should remember that the Board of Transport, as far as I know, could move it to any level it likes. Am I right in that? I mean the grain rates?

MR. SINCLAIR: They cannot now.

MR. EVANS: They could not make it unreasonably low.

THE WITNESS: Well, that is what they are there for, to see that justice is done to everybody concerned.

THE CHAIRMAN: Q. I think that your present state of mind is that any increase in these rates is a matter which might have some effect on the markets.

A. If carried to a certain point, yes.

Q. You say you would not do anything at all without having this consultation, this conference?

A. Yes. I agree with that thoroughly, although I would personally take the responsibility tomorrow, for example, should I be given the responsibility of raising the rates on wheat in Western Canada by several cents per bushel, and I would be confident that I was doing right. But there are the lives of 250,000 families involved in this, so therefore I would like my judgment to be verified by others, and given the most careful consideration.

Q. Does that mean that there should be a reconsideration and special study of that one subject, whether

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or not those rates were changed upwards or downwards, without causing some injury to the raisers of wheat? Is that as far as you are going?

A. I have made a study and I am convinced of it, and I am trying to convince others that that is the situation.

MR. SINCLAIR: Q. Isn't this the position: That irrespective of whether an increase is made, and the fact that the western farmer -- I think the witness' stand is this: That the rates should be compensatory to the rail-ways, should be remunerative, and that if the farmer needs assistance, that that should be done by the government, and not dealing with transportation.

THE CHAIRMAN: That is a matter of policy which really is another consideration.

Mr. Armstrong started by pointing out to us that these rates are really not by any means as important as we think they are.

MR. SINCLAIR: Quite so.

THE CHAIRMAN: And as affecting the world price of wheat, if we could stick to them, we might get somewhere.

MR. SINCLAIR: I think, sir, that he also, if I may recall this, showed that he realizes that there was a very deep rooted feeling among the western farmers that they were of benefit to them. That of course is a factor which must be taken into consideration.

THE CHAIRMAN: He said it was only a superstition.

THE WITNESS: A deep superstition, sir.

MR. SINCLAIR: I think the Canadian Pacific recognizes that there is very deep rooted feeling among western farmers that the Crows Nest Pass rates are to their advantage. But we say that that understanding or feeling of theirs, which I certainly think is there and

is honestly held, is not in accordance with the facts in some circumstances, possibly much of the time, and depending, as I think the witness has pointed out, on how much the transportation factor is raised, and of how great importance it is in the total transportation cost of the movement of grain from the farm to the market in the United Kingdom. The European market is the basic factor, and the International Wheat Market.

THE CHAIRMAN: Q. Mr. Armstrong goes this far: He says that he would increase the rate by a few cents, without any fear or tremor?

A. Quite so.

Q. That means that you think in that case the market would increase by that 3, 4 or 5 cents?

A. I believe that, at the present time.

Q. Do you think it would have any effect on Fort William quotations?

A. This consideration would only arise upon the termination of the present international agreement and the negotiation of a new one, or the re-opening of an open market.

Q. But as you pointed out a while ago, even today the prices are arrived at by negotiation?

A. That is right.

Q. And for very large quantities of wheat; and all these factors are considered. You told us that.

A. That is right.

Q. And you think that an increase of a few cents, as you put it, would not make any difference to the total price?

A. I am confident of that, at the present time.

Q. Is it possible at all to draw a line anywhere and to say that above that line the market would not

absorb it?

A. I would like to spend a few months in Europe and have a look at the condition of the rickyards on European farms.

MR. SINCLAIR: There is this very major factor which must be kept in mind: That the Board of Transport Commissioners, if they had jurisdiction over grain rates, would have to find that they were reasonable, and they could not arbitrarily, and they would not arbitrarily set rates on grain irrespective of reasonableness, irrespective of the reasonableness of those rates; and that would include reasonableness to the western farmer.

THE CHAIRMAN: But if the reasonableness to the western farmer again, as Mr. Armstrong says, if it again resulted in an inadequate rate to the railway, what would you do about it?

MR. SINCLAIR: I would say that the position of the Canadian Pacific, which was every carefully considered, is that the rates, should that situation come about that they are higher, and are reasonable to the railways are higher than would ordinarily be reasonable to the western farmer, then that is a situation in which national policy must come to bear on the situation, and in this situation the western farmer does need assistance.

THE CHAIRMAN: That is just what you said all along.

MR. SINCLAIR: Quite so.

THE CHAIRMAN: Are we getting any further ahead?

MR. SINCLAIR: Except this: I think this witness clearly demonstrates that keeping one segment of the total transportation costs low does not always benefit the western farmer and does not put money in his pocket. I think that is the major point of this evidence.

Consequently, by keeping it low, the Canadian railways are having certain of their revenue drained off by statute and handed to ship owners and dealers outside, or consumers in Europe, or wherever they may be. I think those are two major reasons why we have brought Mr. Armstrong here.

THE CHAIRMAN: I see. You have very many arguments, of course, and one of them is that all freight rates ought to be compensatory?

MR. SINCLAIR: Quite so.

THE CHAIRMAN: But I thought you were starting out to say that freight rates do not really matter to the shipper in this case, and that includes western Canadian wheat.

MR. SINCLAIR: Under some circumstances and much of the time that is true, as long as the rate is not arbitrarily set at some unrealistic level.

I think Mr. Armstrong has made it clear that if the rate is set arbitrarily at some unrealistic level, then, of course, it will have an effect.

I think that is pointed out also by this evidence: That there is one market, an international wheat market; and I shall ask the witness further questions to show that in the United States where the rate has been, we will say, twice as high, that it has not inured to the disadvantage of the American wheat farmer.

I now feel, with that background, that I would like -- and I think it would be helpful to the Commission -- to have Mr. Armstrong's views on some of the statements that have been made in these western rates.

THE CHAIRMAN: Very well, go on.

MR. SINCLAIR: And I would say, and I think it is the most important point which Mr. Armstrong has just

made, that this evidence which we have led now has not been dealt with in these briefs.

THE CHAIRMAN: In what?

MR. SINCLAIR: In these briefs. They do not deal with the economic factor of fixing one sector of the transportation costs. They say that the point the farmer is interested in is the price of wheat, and they leave it at that.

MR. MacPHERSON: That is a matter for argument, and entirely for argument.

THE CHAIRMAN: I would like in the case of the witnesses to confine the evidence to what is really evidence, be it expert or inexpert, in order to furnish the subject-matter of argument at the proper time.

MR. SINCLAIR: That was the sole reason for our calling Mr. Armstrong here and putting this question to him: to bring forth evidence, factual and opinion, based on his experience, which has been over a good many years, namely, the special study of grain, for the help of the Commission.

THE CHAIRMAN: I thought that Mr. Armstrong's thesis as he announced at the beginning was: That the freight rates in Western Canada have, I think he said, nothing to do with the price which the farmer gets for his wheat.

Now he says they are unreasonable. Does that modify the whole proposition which says that the price that the Canadian railway charges on wheat has some effect in the markets?

MR. SINCLAIR: I do not think it has ever been suggested.

THE CHAIRMAN: I mean, has some effect on the producers.

MR SINCLAIR: I do not think, sir, it has ever been suggested by the Canadian Pacific or any of our witnesses at any time.

THE CHAIRMAN: You are proceeding to show that in their statements in some of these briefs those who have compounded the briefs have given wrong reasons for their belief; is that it?

THE WITNESS: Yes.

MR SINCLAIR: What I think, sir, is that these briefs are directed to the effect of the necessity of maintaining these rates by statute; that is point 1. Point 2, also going through these briefs, is that they must remain at their present level; that is point 2. And it is the reasons that they advance in support of that proposition, as I understood your lordship's direction to be, that our evidence on grain was limited to the question as to whether grain rates should be fixed by statute or whether they should be allowed to come within the jurisdiction of the Board. We say they should come within the jurisdiction of the Board; basic to that suggestion, that recommendation of ours, that we are asking the Commission to accept, is the fact that the rates will be reasonable, reasonable to the farmers of Western Canada and reasonable to the railways at the same time.

COMMISSIONER INNIS: Do I assume from that that you are willing to have the Board discuss economic factors, when you talk about reasonableness to the farmers?

MR SINCLAIR: Well, on a matter the size of grain, and especially western grain, I do not think, sir, that you can deal with the problem without giving some effect to what I think are truisms, economic truisms, and

I think that the Board, competent members that they are, can quite easily weigh them.

COMMISSIONER INNIS: You do not think that means a retreat from the position that you generally hold, that the Board ought not to be a planning body?

MR SINCLAIR: Well, sir, when you say that, I recall the Canadian Pacific position has been that rates should be fixed on the value of service principle. Now, the officers of the company who fix rates and the Board must give some effect to considerations such as I am sure you have in mind, Dr. Innis, in fixing what is a reasonable rate, and I do not think, with respect, sir, that I am withdrawing from any position that I have been in or which I have heard the company---

THE CHAIRMAN: If you remove those restrictions on the Board from it, you simply keep the Board then in the position in which it is in respect of freight traffic. It must fix just and reasonable rates. I think then your argument is that that might very well be done without hurting in any way the grain shipper of Western Canada, because, as Mr. Armstrong says, the rates he pays locally to the railway have, I think, no effect on the price from which the Fort William price is regulated, which is the world price in other countries.

Q. Isn't that it?

A. Yes, sir.

MR SINCLAIR: Quite so, with the modifications that he put in, yes, sir.

THE CHAIRMAN: Then, you see, he departs from that now. He says you cannot fix freight rates there unless you first have a conference of all sorts of interested people to make sure that you are not putting them too high. That is going far beyond saying just let the Board

fix them.

MR EVANS: I was going to venture to suggest, with respect, that there is no inconsistency in what Mr. Armstrong has said. What he has said is that rates can be reasonable. Now, he has not said that rates have no effect. We have never asked that anything should take place but that the Board should have the power to decide what is a reasonable rate, in deciding which it would also decide something which is reasonable both to the railway and to the farmer. Mr. Armstrong has never, with respect I suggest, departed from that in principle, and he has not said that no rate would be unreasonable.

THE CHAIRMAN: Well, I thought he came very near to saying that rates were reasonable so long as the wheat continued to travel. As he put it, a dollar a bushel would mean an embargo.

THE WITNESS: That is right.

THE CHAIRMAN: But so long as the wheat does continue to travel, as it does travel today, then the rate cannot be said to be unreasonable. Is that a fair---

MR EVANS: May I answer that? -- because I think that is a question really of law.

THE CHAIRMAN: I am just trying to find out what your case is.

MR EVANS: That is a question of law, it seems to me. The value of service principle is not a principle by which the traffic is charged all it will bear, and the difference between us, sir, I think, is that you have perhaps interpreted---

THE CHAIRMAN: I quite agree with you as to what the value of service means. I am only trying to find out whether Mr. Armstrong is saying in his evidence this, that so long as the wheat continues to go to these markets, then

the rate, the local freight rate, on it cannot be said to be too high, because it is getting to that market.

Q. Is that what you say?

A. Substantially. Mind you, there must come a time at which you see the effect before it becomes a total embargo.

Q. Before what?

A. Before it becomes a total embargo, you see. For example, I said a dollar a bushel on wheat increase in freight rates would probably embargo the sale of Canadian wheat for export. Well, we get into this method of limits -- would ninety-nine cents do it, and so on down, till you come to the point at which we show that there is no effect. Now, the---

Q. That is, effect on shipments?

A. On shipments. That is my difficulty. I cannot tell you the exact point, and I think it is a matter that will have to be very carefully considered, but I did not---

Q. Carefully considered from the point of view of allowing shipments to proceed as they do proceed under the present rates?

A. I would hope myself that the Board of Transport Commissioners would be fully informed on that point by the best expert advice that they could obtain.

Q. Now, can we have this from you, Mr. Armstrong? Am I right in saying that I have gathered from the whole of your evidence that so long as wheat continues to flow out from where it is produced---

A. Freely.

Q. ---westward and eastward---

A. Freely.

Q. ---then it does not really matter how high the freight rates are, because it is going, it is moving, and

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those rates form part of the world price -- now, I have understood you to say that?

A. Yes, that is substantially my argument. Might I make one point for my own protection, and that is this, that I was not the one who originated the idea that the rates would be fixed by the Board with the concurrence of the shippers and the farmers. I merely quoted the fact that I have, that that had been stipulated, hadn't it? Our counsel had agreed.

THE CHAIRMAN: In your brief, the C.P.R. brief, it says that before new rates come into effect there should be careful study and so on.

MR EVANS: That we would expect it. And then you asked from me an undertaking or an agreement that we would agree that we would first go to the Board. May I put this to you, sir, because I do think there is something between us here: When you put to Mr. Armstrong a question in the terms in which you put it, namely, that so long as the wheat moves freely that would be the reasonable level of rates, I have to say this to you, sir, that that---

THE CHAIRMAN: I would not put it in that language, Mr. Evans. So long as the wheat moves reasonably, the meaning of that is that the cost of the transportation is being reflected in the world price, and therefore paid by the importer. There would be no difference to the Canadian shipper. Mr. Armstrong says that is his contention.

THE WITNESS: Yes.

MR EVANS: Yes, but I think there is a very important distinction here, and perhaps I am not making it clearly, but may I put it? Wheat might move freely under a rate which was higher than we needed.

THE CHAIRMAN: Oh, yes, yes.

MR EVANS: That is my point.

THE CHAIRMAN: I think I will not ask the question over again. Mr. Armstrong is very clear; he does not hesitate; he thinks that so long as wheat does move to these markets by rail and by ship, then the price to the original shipper is not affected, because the world price absorbs that.

Q. Isn't that so?

A. Substantially, sir. There is no misunderstanding if it is put in those terms.

MR EVANS: I just wanted to get that other limit in there.

THE CHAIRMAN: Yes, I know very well, Mr. Evans, the value of service, when you got down to that point, that would be fixed by the Board.

MR MACPHERSON: There was another question that Dr. Innis asked, whether the Board at that stage could give consideration to economic conditions at the time.

THE CHAIRMAN: The question is whether the Canadian Pacific advocates that policy; that is the point, isn't it?

MR SINCLAIR: We are not advocating economic planning, no, but the point is that a factor in fixing a reasonable rate is to consider what would be reasonable in view of all these factors -- the volume of the traffic, the value of it, the value of the commodity, how it loads, density, empty movements; all those factors would have to be taken into consideration.

THE CHAIRMAN: That is, traffic factors.

MR SINCLAIR: Traffic factors and value factors -- what the commodity is worth.

THE CHAIRMAN: I mean traffic factors making up

the value of the service.

MR SINCLAIR: Yes, plus the value of the commodity itself.

COMMISSIONER INNIS: Mr. Armstrong spent some time on these poor devils, the marginal wheat growers.

Q. Now, I assume that any reasonableness established would in your view be in the interests of efficiency and probably weeding them out, which comes as near economic planning as one could---

A. May I say to that, Dr. Innis -- you see, there is nothing new here. All freight rates are fixed in this way, as far as the market factors enter into it. This is a market factor. It is all the same. We are always talking about that. Mr. Jefferson has to keep in mind, you know, all these factors.

Q. We are always talking about it, but we are always denying it is to be included in the discussion.

A. Well, I do not want to prejudice the position taken by counsel here, because really this is not my story, that part of it, but it does seem to me that what we have tried to do in this connection is to fix rates, all the time keeping in mind the maximization of traffic as a means of developing the nation and developing our own business. We are in the cartage business, you know, and we cannot afford to overcharge the customers.

Q. Yes, you and I seem to be very close together, but that does not seem to be the C.P.R. position.

A. Oh, I don't think so.

MR EVANS: I venture to say, sir, that there is no real difference.

THE WITNESS: Oh, no.

MR EVANS: It does not seem to me that because you get an economic result it presupposes an economic plan.

THE WITNESS: That is it.

MR EVANS: If you apply or permit the Board to apply proper principles, it does not mean the Board has economic planning powers. It may have economic results -- we grant that -- but it seems to me a very different thing when you speak of economic planning, because when you plan from the top, as it were, for an economy of a particular kind, it seems to me that by that you infer that the plan brushes aside other considerations that normally might be given effect to in a free economy. Now, perhaps I have not made that clear, but, as I see it, there is no conflict in our position on that.

THE WITNESS: No.

MR FRAWLEY: My lord, might I--

THE CHAIRMAN: Just one more thing: If the effect of these higher rates is not prejudicial to the shipper, it would have to apply to the marginal shipper as well as the other one, wouldn't it -- apply to them all? It does not affect the price.

MR EVANS: Doesn't it get down to this, that---

THE CHAIRMAN: I mean the danger of his being squeezed out.

MR EVANS: Yes. He was only gotten in there under a sort of representation that he would forever have the advantage of an uneconomic freight rate, and is that or is it not---

THE CHAIRMAN: But you are saying that it is an advantage when you put it that way.

MR EVANS: No, sir. What I am saying is that if an uneconomic producer on sub-marginal lands has existed only because he is living off the rest of the economy unnecessarily, then must we perpetuate---

THE CHAIRMAN: I do not see how your increase of

freight rates, with the innocuous result which Mr. Armstrong says it would have, is going to affect any particular grade of farmer one way or the other, the marginal as well as the other. If the price increases accordingly, then they are all on the same footing that they were before, are they not?

MR EVANS: I think Mr. Armstrong said that in a weak market these low rates -- and I hope I am interpreting him correctly -- had produced a tendency for some sub-marginal farming, and I think he did say that that might not always be desirable.

THE CHAIRMAN: Well, that can only mean, then, that the low rates had added to the price, which is precisely the thing which he contradicts in his evidence.

MR EVANS: In a weak market. That is certainly an economic question that Mr. Armstrong might answer.

THE WITNESS: The point is this: You have to consider the competitive effect of the presence of these sub-marginal operators. Freight rates, being part of the cost of production, do have a market effect. I am saying that the market effect will be absorbed by the consumer in a weak market within a very wide range of prices. Now, for example, if you raise these freight rates at all, it is quite possible that at some particular time, particularly in a strong market, the inclination will be for the buyer to mutiny a little bit and say, "Well, I won't pay any more than this," you see, so that there is a market effect out of the increase in any cost -- there is bound to be -- and all I am trying to say is that the market effect has been exaggerated in the first place, and in the second place that in a weak market, when protection for the farmer is so necessary, you do not get protection for him by means of this, but I do say that if you keep the freight rates lower than they should be you are probably subsidizing your

marginal and inefficient farmers, particularly in times of strong markets.

COMMISSIONER ANGUS: Q. Are you contemplating a rate being fixed for a relatively long period during which markets will be weak and strong and weak again, or being under continuous review?

A. Professor Angus, I have an idea that they are going to be kept under continuous review, never mind what I say about it. You see my point. The point is that this is such a big factor in our economy that I cannot contemplate the circumstances in which a major change in the wheat market, of a cyclical kind -- I do not mean just a temporary daily or monthly fluctuation, but a major, a cyclical trend developing, you know -- I do not think that the minute you got that, I do not think there is any doubt in the world that you are going to hear from one party to this agreement, saying that the price is now too low or the rate is now too low or too high for circumstances as they are. You will have this argument all over again, and I suppose that we will disagree, as we may disagree now, but I think that is the greatest weakness of the so-called Crows Nest rates, that they have been in effect since 1897, the fact that in the greatest range of prices that the wheat market is ever likely to see they have been in effect on a uniform basis.

COMMISSIONER INNIS: Q. Yes, but you attract these settlers into sub-marginal land by statute, and then you proceed to chase them out with scorpions by the Board of Transport Commissioners.

A. Well, I have told you, you know, that there is a delicate sociological question, and we may have to get a very competent board of adjustment to deal with the marginal

cases. It is a delicate question.

MR SINCLAIR: Of course, we are not suggesting, Dr. Innis, that there is a large marginal production of grain in Western Canada.

THE WITNESS: Oh, no. There is some.

MR SINCLAIR: We are not suggesting that at all.

THE WITNESS: There is some.

THE CHAIRMAN: I do not see how anything that can affect the price of this product to the marginal farmer will not at the same time affect the price of the same product to the other farmer who is not marginal.

THE WITNESS: I pointed out what would happen in a strong market, you see.

THE CHAIRMAN: Well, we will adjourn now.

---The Commission adjourned at 1:00 p.m., to meet again at 2:45 p.m.

Ottawa, Ontario,
Wednesday, March 15, 1950.

A F T E R N O O N S E S S I O N

P. C. ARMSTRONG, Recalled

THE CHAIRMAN: Mr. Sinclair, before you begin your examination, there were some figures quoted this morning which may be accepted as authentic, and I think I am going to make some corrections now. It was in discussion between you and Mr. Armstrong.

Q. You remember we were talking about the importations of Canadian wheat?

A. Yes, sir.

Q. Well, I find according to this report that in that year, 1936 and '37, there were in round figures 92 million bushels of Canadian wheat imported into Great Britain.

A. And retained, sir?

Q. No.

A. Not retained?

Q. No; a great deal was unloaded in Liverpool, you see, or other ports and then transshipped. Then on the continent, the figures as to what was retained in the respective countries, consumed there: We find that there were 16 million bushels retained and consumed in Belgium, where the population was only about 8 million, you see.

A. Right, sir.

Q. Which per head is a larger consumption of Canadian wheat, I think, than in any country except Scotland.

A. Yes, sir.

THE CHAIRMAN: My great regret is, there were not enough Scotsmen. They insisted on bread made out of flour that had 95 per cent Canadian wheat in it -- the finest

bread in the world, I think.

MR MACPHERSON: They didn't want any cake, my lord.

THE CHAIRMAN: They had bannocks too, you know.

MR SINCLAIR: And oatcakes too, sir.

THE CHAIRMAN: Oh, yes, oatcakes.

EXAMINATION CONT'D BY MR SINCLAIR:

Q. Just before the noon adjournment, Mr. Armstrong, we were discussing the statement at the top of page 20 of the brief of the Prairie Provinces on the grain rates, and you were dealing with the fact that in your view transportation charges on rail movement of grain averaging 12¢ per bushel were not a major factor in deciding the economic fate of Western Canada; I would ask you if you would not mind to see if you could put that statement in this brief in possibly clearer focus?

THE CHAIRMAN: Is that the Saskatchewan brief?

MR SINCLAIR: The brief of the three Prairie Provinces; they have a joint brief, my lord, the three Prairie Provinces.

THE CHAIRMAN: You mean on the Crows Nest?

MR SINCLAIR: On the Crows Nest, yes.

THE WITNESS: The statement is that any alteration in Crows Nest grain rates would be ruinous to the wheat-growing areas.

THE CHAIRMAN: Q. Any what?

A. Alteration in the Crows Nest rates -- I presume that they meant upwards -- would be ruinous to the wheat-growing areas. Now, does anyone imagine that an increase of a few cents per bushel in the rates would destroy the grain-growing economy of Western Canada, when it is well known that the economy has been subjected for quite other

reasons to fluctuations of its fortunes which have to be measured in terms of something up to one dollar per bushel?

MR SINCLAIR: Q. Mr. Armstrong, would you right at this point give the Commission your view as to the fluctuations in price on the western farm prosperity?

A. Well---

THE CHAIRMAN: Fluctuations in price?

MR SINCLAIR: In price, the price of wheat. Mr. Armstrong said it was subject to broad fluctuations, and I asked him to give us his views as to the effect of such fluctuations on western farm prosperity.

THE WITNESS: Farmers in Western Canada are by the very nature of their environment and occupation exposed to remarkable fluctuations in fortune, vicissitudes of fortune, but I would like to point out that they have prospered under conditions in which the wheat market has fluctuated by more than 12¢ a bushel in a short period.

Q. What would you call a short period?

A. Well, within a month we have seen the rates rise and fall frequently more than 12¢ per bushel.

Q. You mean the cash price of grain?

A. The cash price of grain.

Q. Yes?

A. The result is that they were not wiped out because this happened. I have seen farmers, on the other hand, reduced to desperate poverty at a time when the price of wheat was barely fluctuating at all and with the freight rates absolutely stable as they have been. So I can only say that I cannot see that---

THE CHAIRMAN: Q. Pardon me. You did not tell us what the price was, the low price?

A. In the depression, sir. Sometimes in the depression the price remained for long periods practically stable,

at very low and distressing figures, and freight rates remained stable, and the farmers were reduced to poverty. So I regard this statement as so exaggerated, the statement that the whole fate of Western Canada depends on the Crows Nest rates, that it is of no value at all as economic argument. And yet, peculiarly enough, except for this statement---

THE CHAIRMAN: It is advanced to us by economists.

MR SINCLAIR: I think that this is advanced by the provinces. Their brief does not disclose who the author of it is.

THE CHAIRMAN: Well, didn't we have, for instance, Dr. Britnell here from Saskatchewan?

MR MACPHERSON: Dr. Britnell gave evidence to the same effect.

THE CHAIRMAN: He read this brief for you?

MR MACPHERSON: Not this one, my lord; this is one that has not been in yet.

THE CHAIRMAN: The one that I have, which is the Saskatchewan brief, he read that one.

MR MACPHERSON: He read that one.

THE CHAIRMAN: And he was questioned on it. That one puts the situation -- we cannot avoid looking at it, because it is basic to the discussion -- that the production of the province nets its producers the world price less freight to world markets -- you hear that statement -- while at the same time goods purchased in the province cost the purchaser the world price plus transportation costs from the point of origin. Dr. Britnell was questioned on that, and he would not allow of any variation. He said that the wheat producer does pay the cost of transporting his wheat to the world market altogether.

MR SINCLAIR: I think sir, that you asked him or

Dr. Hope -- I am not quite sure which -- whether it was not true that the people in Great Britain believed that they paid the transportation costs on wheat.

THE CHAIRMAN: Yes; when I was over there, the economists over there, speaking for the millers, took the directly opposite view. They say that the importer pays the whole of the cost, including transportation cost, for what is their raw material.

THE WITNESS: Could I offer a sort of summary---

THE CHAIRMAN: That is, those speaking to me in England spoke as you do; they say, "No, we pay the cost of that transportation. If my mill were in Saskatoon I would get the same wheat for the price that the Maple Leaf Mill gets it, or the Quaker Oats."

MR SINCLAIR: Of course, I think, sir, this statement in the brief, which goes directly towards Crows Nest, points up this view.

THE CHAIRMAN: Yes, I know, but the Crows Nest is a part of the cost of transportation; I mean, the rates paid under the Crows Nest statute are a part of the cost of transportation.

MR SINCLAIR: Quite so.

THE CHAIRMAN: For instance, Dr. Britnell says that all those costs are paid by the shipper of wheat.

MR SINCLAIR: Well, I have no doubt that Dr. Britnell will be back.

THE CHAIRMAN: And another school of economists says, "No, they are paid by the European importer of wheat." Now, I am just saying we could discuss that interminably, could we not?

MR SINCLAIR: Well, sir, I imagine that Dr. Britnell or someone will be presenting this brief, and one of our thoughts---

THE CHAIRMAN: He will be presenting the Crows Nest Pass brief?

MR SINCLAIR: Yes, and one of our thoughts in putting forward the views that we are now, would be that our friends from the provinces and their experts would be able to see them, and then we will have the opportunity of asking them whether they have given, in some of the statements they made, full consideration, or shall I say weight, to some of these factors that we think are pretty basic economic factors.

THE CHAIRMAN: Well, I am not trying to shut you off at all. I am just saying that we have here experts on both sides of that very question, haven't we, as to who is paying the cost of transportation?

MR SINCLAIR: Quite so.

THE WITNESS: May I offer a suggestion, sir, there? -- that this is one of those great adventures in semantics, in the meaning of language.

THE CHAIRMAN: Well, no, it is more than the meaning of language.

THE WITNESS: Well, there is quite a point there, sir. What I am trying to say is this: It is perfectly true that the western farmer gets net the price on the world market less the cost of transportation -- he always does get that -- but what I am trying to say is that there is a suggestion that the cost of transportation plays a part in setting the world price, which I think is exaggerated, you see. I think you have to start out---

THE CHAIRMAN: You had better take the language as it is. He says that the farmer or the producer gets the world price -- that is, the man in Saskatchewan gets the world price -- less freight to world markets. Now, that is the bald statement.

THE WITNESS: My only qualification, sir, is that that is true, but it does not follow from that that an increase or decrease in transportation will be reflected in the net price to the farmer. It may be reflected in an increase or decrease of the world price at the other end. You see the difference of approach.

THE CHAIRMAN: Yes; that is your modification.

THE WITNESS: Yes.

MR SINCLAIR: Of course, that statement, as I understand the witness, may be on its face quite acceptable and correct, except that the price at Fort William has adjusted itself to the factors that are elements in---

THE CHAIRMAN: You mean the statement I was referring to?

MR SINCLAIR: Yes, with that explanation.

THE CHAIRMAN: It is not admitted overseas. The man overseas says that naturally this is his raw material, and his factory is over there, and he has to pay to move it over.

MR SINCLAIR: He, of course, says what Mr. Armstrong says, and that is that the price at Fort William is a mere function of the international wheat market, and it is just a convenient---

THE CHAIRMAN: Then the whole question is, does or does not the variation in the cost of transportation affect the price which the grower of the grain receives? Apparently you are endeavouring to show that it does not, at least within what you now call reasonable limits. Is that right?

THE WITNESS: That is right.

MR SINCLAIR: Sir, Mr. Armstrong gave evidence this morning about what happened in the United States when they put those emergency rates in.

THE CHAIRMAN: Yes; on a certain occasion freight rates were lowered, and the next day wheat went down.

MR SINCLAIR: And when they were raised again wheat went up.

THE CHAIRMAN: But they did not stay down; they went up again, and attained their very highest peak that summer.

THE WITNESS: They attained a peak that summer, sir, of that period.

THE CHAIRMAN: So what can you deduce from that? I am just trying to show---

MR SINCLAIR: The immediate reaction is our point.

THE CHAIRMAN: I do not want to argue; I am trying to show how we could pass interminable days and weeks and months.

MR SINCLAIR: Sir, with great respect to my friends and the briefs that they have submitted, we are trying to make a close analysis of it, and there is not very much you can look at.

THE CHAIRMAN: I would like for us to be told where Mr. Armstrong disagrees with anything or agrees with anything that Mr. Sinclair may read to him out of these briefs.

MR SINCLAIR: And we, of course, hope that these people who are presenting these briefs will do a more shall I say thorough job on the economics behind some of the statements that are made here.

THE CHAIRMAN: All right, then.

MR MACPHERSON: Whether a thorough job is done or not, of course---

THE CHAIRMAN: I beg your pardon?

MR MACPHERSON: My friend suggests that we should

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do a more thorough job. That again introduces a question. It is a question of opinion as to whether a thorough job has been done or not.

MR SINCLAIR: Well, if my friend is sensitive, evidence can be adduced in support of the general statements made in the brief.

Q. Now would you look at page 28, Mr. Armstrong, of the brief of the three Prairie Provinces? The contention there put forward in the first paragraph---

THE CHAIRMAN: Now are you referring to the Crows Nest brief?

MR SINCLAIR: Yes. I am only directing the witness' attention to this specific---

THE CHAIRMAN: What page do you refer to?

MR SINCLAIR: Page 28, my lord; and I am asking him to direct his attention to the contention put forward at the top of page 28, that there can be no comparison between conditions in Western Canada and the spring wheat area of the United States, because the United States does not export any spring wheat except by a process of dumping.

Q. I would like your comment on that.

THE CHAIRMAN: Pardon me. My attention was drawn away. Show me where it is.

MR SINCLAIR: I have re-phrased the argument that is put at the top of page 28.

THE WITNESS: I think this whole argument reflects a complete misunderstanding. Except as far as governmental interference in recent years has affected United States wheat prices, these prices have been set in open markets -- in fact, even with the governmental interference they are still set in open markets -- and spring and fall wheat are sold on those markets competitively with each other. The situation has always been one in which, since the United States produces

a much larger quantity of fall wheat than spring wheat, and since the United States is a very wealthy nation with a high standard of living, naturally tending to retain the highest quality of milling wheat for domestic consumption, the volume of exports of fall wheat of course will be enormously greater than those of spring wheat; in fact there will be very little spring wheat exported.

MR SINCLAIR: Q. Mr. Armstrong, when Mr. MacPherson was cross-examining Mr. Jefferson I think he made a distinction between winter wheat and spring wheat?

A. Well, I will call it winter wheat, then; it is the same thing. Now, the point is this, that if it were true that there was a domestic market for spring wheat in the United States and an export market for winter wheat, and they were two different markets, you would have to start off with the assumption, of course, that the entire domestic market was filled by spring wheat. Now, the total spring wheat crop of the United States is probably -- I will have to look the figures up again, but I will risk the statement -- it is not more than half big enough to provide for the domestic use of flour in the United States, so the rest of the flour in the United States which is used domestically must come out of winter wheat -- there is nowhere else for it to come from -- so that you have got a single market for these two wheats -- a single market. There are spreads between them -- there is always a certain normal spread between this grade and that grade, this type and that type -- but there is one market. If the price of spring wheat in the United States is increased, it is accompanied by an increase in the price of winter wheat, and vice versa. It is not a case of there being two markets.

Q. Is it correct to say, therefore, that you are taking issue with one of the basic arguments in this brief, that

there are two markets?

A. Direct issue; and I hope to explore that a little more fully later on. Now, there is another point in this connection. This argument is introduced and built up, obviously with in mind the idea that because the spring wheat of the United States is largely used in the domestic market, therefore it does not begin to pay as much freight rates as our wheat which has to go to export markets. You see, it is grown in the United States, and it is a domestic market, so therefore it is grown close to where it is going to be used.

THE CHAIRMAN: Q. The haul is shorter, of course.

A. I would like to explain that.

MR SINCLAIR: Q. This is the contention put forward by this brief?

A. That is the contention. I want to point out first of all that as far as domestic consumption and export are concerned in both Canada and the United States all the wheat that goes as far as the Head of the Lakes, Fort William or Duluth, in either country, is carried in each country at the same rates whether it be domestic or export. That is, all the wheat going to Fort William in Canada, regardless of its further destination, is carried at the same rate; all the wheat going to Duluth in the United States for furtherance is carried at the same rate, a much higher rate than that in Canada.

(Page 18153 follows)

Q. What you mean is whether the wheat that goes to Fort William is milled and baked into bread in Toronto or Montreal, to Fort William it carries the same rate whether subsequent to its arrival at Fort William, some goes to England and some to the United States?

A. At different rates in the United States, much higher.

The point is that there seems to be a sort of a thinking that because the farmer in North Dakota sells his wheat to be consumed in the United States and not abroad, that that is equivalent to saying that he sells it to be consumed in the next village. In most cases he sells in the great population centres of the Eastern United States, and most of the Spring wheat in the United States, which is consumed in the domestic market of the United States, moves via Duluth, the Great Lakes, Buffalo to the domestic market in the United States, as long a distance as our wheat moves to Montreal for export, or almost as long a distance, and at rates which are very much higher than those in Canada.

Q.
THE CHAIRMAN: When you say "consumed" are you talking now of the eater of bread or the miller?

A. The eater of bread.

Q. A great many of these United States mills are right there in the West, are they not, in Minneapolis and St. Paul?

A. I hope to explore that a little more fully later on.

Q. That is as far as the wheat in question goes.

A. I will explore that, but wheat moving to Minneapolis to be milled and forwarded pays the milling

in transit rate, which is much higher than the corresponding rates in Canada, and much higher than the export rate in the United States.

MR. SINCLAIR: Q. In other words, the domestic rates locally in the United States are higher than the export rates just as they are in Canada?

A. Yes, that is right. Now, this whole argument can be answered by the simple fact that the wheat from the Spring wheat states of the Union, whether it be going for export, or domestic market, before it reaches the termination of its journey has paid very much higher rates than has the wheat ^{from} Western Canada which reaches the termination of its journey in the elevators at Montreal, Saint John or Halifax, so that the fact that there is a large market for Spring wheat in the United States does not reduce the burden of transportation charges on Spring wheat to any extent. Now, this brief points out my previous argument that whether it be Spring wheat or Winter wheat, United States wheat or Canadian wheat, export or for domestic consumption, wheat grown in the United States and marketed under the policy which establishes wheat prices in that country is more remunerative to the grower at ^{the} present time than wheat grown in Canada and marketed under the policy prevailing here, despite the fact that wheat movement in the United States, whether for export or domestic purposes, pays much higher rates than in Canada. In short, the brief on this point demonstrates more clearly than I possibly could have, the unimportance of freight rates as a factor in determining the income of the wheat farmer.

THE CHAIRMAN: Q. You say, unimportance of freight rates?

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A. Yes, the unimportance of freight rates.

It would be very amazing to me to hear the views of growers of Spring wheat in the United States as to the suggestion that the fact that their product is chiefly used in the domestic market places them in a much happier position than the growers of Fall wheat, which is exported. They do not think so.

MR. SINCLAIR: Q. Will you turn to page 29 of the three provinces' brief on grain and in the first complete paragraph you will note there the argument or suggestion that it is important to remember that fifty per cent of the Spring wheat crop of the United States moves an average of four hundred and fifty miles to a lake terminal, while the average haul in Canada is seven hundred and seventy miles.

A. There seems to be some confusion in this thinking. It is of no importance whatever to the wheat economy, however important it may be to the railways, how many miles wheat is hauled. The only economic question is how much is the freight rate? The wheat from North Dakota moving an average of four hundred and fifty miles to Lakehead pays an average -- this cannot be calculated with precision, but I am willing to submit this estimate to examination -- of somewhere around 38.5 cents ^{per hundred pounds} from points in North Dakota to the Lakehead at Duluth, to which, 50 per cent of all the Spring wheat of the prairie states of the Union moves. Now, turning to Saskatchewan, just as 50 per cent of the United States Spring wheat crop is grown in North Dakota, so is 50 per cent of the Canadian prairie crop grown in Saskatchewan. Now, I agree that moves

a distance of seven hundred to eight hundred miles, instead of the four hundred and fifty miles in the United States, but the Saskatchewan wheat pays an average rate of 20 cents per hundred pounds as compared with 38.5 cents for the North Dakota wheat.

MR. SINCLAIR: Q. I think it might be of interest to the Commission that on page 94 of the Appendix to Part I of the Canadian Pacific brief that point Milroy North Dakota is shown, and the rate from Milroy to Duluth is 38.5 cents and the distance from Milroy North Dakota, where the rate is 38.5 cents, to Duluth, is 469 miles.

Yes, Mr. Armstrong.

A. Now, this may all be very hard on the Canadian railways. They have to face the situation of drawing wheat twice as far for half the rate, but surely it is improper to suggest that it imposes an unfair burden on the Canadian wheat grower as compared with his colleague in the United States.

Q. Now, if you will go back to page 3 of this three prairie provinces' brief on grain, in the first complete paragraph on page 3, I draw your attention to the statement and I quote it:

"The Crow's Nest rate reductions as a group, therefore, were clearly directed toward the furtherance of economic development in the Prairie region and toward the linking of that development with the Eastern Canadian economy."

Do you agree with that statement?

A. There cannot be the least ^{doubt} about the truth of this in the circumstances of the time, and with some probable exaggeration of the value of these lower rates

on wheat. It is agreed that the government of Canada intended the former Crow's Nest Agreement to play an important part in encouraging development of the prairies, but it is a mistake in my opinion to draw from this the conclusion that this was the only purpose of the agreement. In fact, the brief of the prairie provinces is very clear on this point, that brief suggests that the government was definitely moved also by a desire to guarantee the economic development of southern British Columbia as part of Canada.

MR. SINCLAIR: Those statements are to be found on pages 6 and also 8 of the brief.

A. There was clear danger at that time, and if history is well written, there certainly was real danger that without the construction of a railway through the Crow's Nest Pass, that area might have become economically and even politically annexed to the United States. The best evidence on this point I have ever been able to obtain I got from the brief of the provinces. In paragraph 2 on page 12 of the same brief it quotes a statement by Sir Richard Cartwright, who was, I think, Minister of Finance, but he was certainly speaking for the government.

THE CHAIRMAN: Q. When was this?

A. 1897.

Q. I remember he was Minister of Trade and Commerce.

A. He was defending the Crow's Nest Agreement. This is what he said:

" . . . we give, if you choose to call it, some \$5,000 to \$6,000 per mile to the Canadian Pacific railway for constructing this line, and we are paying them a further sum of \$5,000

or \$6,000 in return for valuable privileges to the whole Northwest and Eastern Canada as well."

Sir

You see, what/Richard Cartwright said there in plain words was that half of the payments made to the Canadian Pacific under the agreement were intended to obtain construction of the railway and only half of them were in compensation for rate reductions. I suggest that this should be kept in mind in discussing the benefits which C.P.R. is so often alleged to have received from this Crow's Nest Agreement.

THE CHAIRMAN: Q. When he said "in return for valuable privileges" --

A. The context I think sir, in the debate will show he is making this distinction: you had to build the railway for one purpose, so half the subsidy was for that purpose, and you got concessions on rates, valuable privileges, you see, for which you paid the other half of the subsidy.

I think it ought to be remembered that only half of the subsidy went in for rates.

MR. SINCLAIR: Q. That is of interest in assessing the historical significance of some of the statements made in that brief?

A. Yes.

Q. I would ask you now to turn to the brief of the Pools, that is, the Manitoba Pool Elevators, the Alberta Wheat Pool, and the Saskatchewan Co-operative Producers.

Now, have you read this brief, Mr. Armstrong?

A. With care, Mr. Sinclair.

Q. I would ask you to turn to page 9 of that brief, and in the last full paragraph on that page right at the bottom, I would first ask you to direct your attention

to the suggestion, the argument, that there should be no connection between the freight rate on grain and its market price, and I would ask you to let me have your comments on that point?

A. Well, broadly speaking, it would be impossible . .

THE CHAIRMAN: Q. Who says this?

MR. SINCLAIR: This is the Pools' brief, sir.

THE WITNESS: Now, broadly speaking, it would be impossible to maintain at all times a close relationship between the market price of grain and the freight rate on it. It is an accepted principle that freight rates should take into consideration the value of the commodities carried within certain limits which Mr. Evans has so often stressed. But that is only one factor. Another factor is the compensatory nature of rates.

THE CHAIRMAN: Yes.

THE WITNESS: It must be evident that when there is a general increase in price level the operating cost of railways will rise, and when there is a general fall in price levels, operating costs of railways will fall. Other factors also will affect the operating costs of railways. As the volume of traffic increases, it will usually be possible for them to render service at a unit cost which will be lower than would prevail with a smaller volume of traffic.

(Page 18162 follows)

Thus it is impossible to establish a fixed rule that transportation rates must automatically rise and fall with fluctuations in the general price level. But there must be some such general relationship.

MR. SINCLAIR: Q. I would ask you to turn your attention, and let us have your views, on the assertion on page 9, in the last complete paragraph which says:-

"The present wheat price is entirely due to the aftermath of a great war."

A. I would hope that this is wrong.

Q. That is the third sentence in the last complete paragraph on page 9.

A. In the first place, everyone is going to agree that out of the war, and out of the methods of public financing followed during the war, and under the stress of a great war there has been an almost universal debasement of the currency in this and in other countries.

That is something which often happens during wars. You can do it by cutting down the amount of gold in the gold sovereign. You can do it by printing money in one form or another; and you can do it by quite ingenious operations concerning the national credit.

But this debasement of the currency has involved an inevitable increase in the price levels, and it may well be a permanent general increase to some extent. I do not say that the whole increase will necessarily be maintained, but there are some good reasons for thinking that some of it is going to be maintained.

The Food and Agriculture Organization is highly respected by the pools, and that organization has taken a very definite stand.

Q. That is an organization of the United Nations?

A. Yes, it is an organization of the United Nations, and it has taken a very definite stand to the effect that the world faces an increasing shortage of food.

I have here a clipping taken from the Montreal Standard of March 12, 1950. It is a press dispatch from Washington dated March 11.

Sir Herbert Broadley, the Deputy Director General of the F.A.O. used these figures:-

"Before the war 22% of the population received a submarginal supply of 2000 calories a day or less."

That is, 22% of the world were obviously underfed by his standards.

"Now, that underfed proportion has risen to 35%.

In 1939 50% of the world's population received the barely adequate supply of 2,240 calories a day. Now, this same proportion has dropped just below adequacy - to 2,100 calories or less.

It is certain that 80% of the entire world's population is getting less protein than before the war."

And the general statement is made:-

"The world's food supply is becoming less adequate for an increasing and always underfed population."

Objection may be made to this that the fact that people need food does not mean that we shall be able

to sell to them. But do not let us be defeatists.

Let us assume that modern civilization is going to continue, and that modern civilization is not going to continue unless we find some method of tracking-down the present obstacles to an easier exchange of commerce between nations.

Q. I direct your attention particularly to this last complete paragraph where the statement is made.

THE CHAIRMAN: You say that modern conditions - are you hopeful that in the future some things we have been reading about such as the potato crop in the United States will not be repeated?

A. I certainly hope so.

Q. There are a lot of eatables of a very specific kind which are being destroyed?

A. To discuss the potato situation very briefly - -

Q. I just use it to show that despite your optimism - -

A. That is not a case in contradiction; and in that case the United States government decided to pay the farmers a much higher price for potatoes than the situation warranted. And the surplus was created for that reason. The potatoes did not move very well.

Q. They cannot get to the relief of these under-nourished people anywhere?

A. Not potatoes. I think that if the United States has any money to use for relief it had better use it for wheat and for other goods which are more readily transported and stored than are potatoes.

COMMISSIONER ANGUS: The basic doctrine of the Food and Agriculture Organization pointed out that the real cause of want was poverty and rather suggested that the

people who are underfed have nothing which they could give in exchange for food.

A. Until we have explored, Professor Angus, the restoration of some method of procuring an interchange of commodities, a better method than now exists, we do not know what they could do.

We do not know at the present if those people are really doomed to perpetual poverty unless relieved by charity, something which ought to be done in any case; or whether given an opportunity to enter markets and to procure methods of interchange better than those now existing, they might not be able to survive. But I think that is getting a little philosophical, is it not?

MR. SINCLAIR: If that meets the question you raise, sir?

THE CHAIRMAN: I beg your pardon?

MR. SINCLAIR: If what Mr. Armstrong has said meets the question raised, I would ask him to turn his attention to the statement in that short paragraph where it was suggested that the farmer pays the freight to Fort William. What have you to say about that?

THE WITNESS: We discussed it at some length this morning. I do not believe it.

THE CHAIRMAN: Q. Between those two postulates: on the one hand we say the farmer pays the freight, and on the other hand we think he does not, but that the exporter pays it. Now, is there not some middle ground where people could meet?

Is there not a possible economic law which could be set down?

You warned us about trying to state any economic law in

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5. The fifth part of the report deals with the summary of the work during the year. It is divided into two main sections: the first section deals with the summary of the work in the field of research and the second section deals with the summary of the work in the field of education.

one sentence; yet here we have two or three sentences and they do not agree.

You told us a while ago that this factor of freight rates was unimportant. Now, can you give us a formula to get out of it?

A. My statement was very carefully made, you know, sir.

At the bottom of a buyer's market, when the farmer is being pushed down to the bottom price which he will take, he pays no freight rate at all. The other man pays it.

But at the top of a seller's market, when the farmer is not at all sure, he himself pays a good deal of the freight rate, all he can afford.

Q. He does that although the demand for it must be much greater for it in the market?

A. When the demand is greater, it is probable that the buyer does not pay as much of the freight rate as when the demand is very poor.

Q. I thought to the contrary. When the market was 26¢, Mr. Brown charged you 2 ¢ a dozen to bring the eggs in. But when the market was 20¢ he only charged you 1¢.

A. Nothing at all. He ^{tried to} charge him nothing.

Q. But we are not arguing that the railways should go that far.

A. Let us examine the conditions of 1932, which some of us at least will remember, when wheat fell to 38½¢ a bushel one day at Fort William. Hard hearted buyers would drive the market. We do not doubt that buyers of Canadian wheat in other countries have been pretty hard hearted in their attitude to price. But that was their business. They wanted wheat cheaply.

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Now, if at that time the average freight rate on wheat in Western Canada had been cut from 12¢ to 6¢ per bushel, I say that the only result would have been to reduce the bottom price to 36½¢ instead of 38½¢, because the farmer would still have got as much at his country elevator with a 32½¢ price and a 6¢ freight rate as he got at the country elevator with a 38½¢ price and a 12¢ freight rate.

You would not have hurt the farmer. You would simply have handed a bonus from the Canadian railways or from the Canadian taxpayers, whoever brought about this reduction in the freight rates, to the foreign buyer who was already buying wheat as the cheapest commodity ever sold in modern history.

Q. Is that an argument?

A. My Chicago case was intended to demonstrate the accuracy with which you can forecast that fact. That was what happened in Chicago in 1929. You did not help the farmer. He continued to get the same price.

Q. Well, for a while.

A. The world market conditions of course - you have to remember the world market conditions will have been merely a minor factor.

MR. SINCLAIR: It is merely underlined.

THE CHAIRMAN: I want to see if there is any difference between the facts and the argument.

MR. SINCLAIR: We have called Mr. Armstrong as an expert and as a serious student of a very difficult and very complex situation, the marketing of grain.

THE CHAIRMAN: He says that if you do certain things to the freight rates, then certain things will happen to the prices.

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MR. SINCLAIR: Yes.

THE CHAIRMAN: That was only one instance.

MR. SINCLAIR: I think his point is demonstrated: that the narrow factor of the rail transportation in wheat is a minor factor in the price of wheat and is ever retained by so much greater consideration and so much basic factors than would be the small factor of total transportation cost.

THE WITNESS: Let me go back to my 1932 case.

If you would reduce the freight rates, then it would have fallen at the moment of the reduction; and if you had increased the freight rates, it would have increased at the moment of the increase?

THE CHAIRMAN: The price, you mean?

A. Yes, the price at Fort William.

Q. And you state that as a positive fact?

A. I am confident about it. I am giving it as an opinion, but as a very firm opinion.

It was not going to stay at $38\frac{1}{2}$ cents. It rebounded to somewhere around 62¢.

My point was that it was going to stay at the minimum which the buyer could get the seller to accept.

MR. SINCLAIR: Q. And that idea suggests using the American example and it points out again and underlines your philosophy that in the United States the price did go up after it was reduced. But it was not the effect of manipulating the freight rates that did it on the up-swing.

A. As a matter of fact, Mr. Sinclair, the price would have risen that much higher if the price had not been reduced. That is the point.

Q. And the effect of the freight rates being raised

and pushing the price, is demonstrated by what happened.

A. Some five months after, yes.

Q. Now I shall read to you from the very bottom of page 9 and the top of page 10 from the Pool Brief where I find this:-

"The Company..."

Meaning the Canadian Pacific...

"...further says that should it ever come about that the maximum set by the agreement should prove inadequate to return the Company a profit, then all other shippers must make up the deficiency. Any application based on that contention should not be considered until all other sources of revenue have been exhausted."

I would ask Mr. Armstrong to let us have his comments on that.

THE CHAIRMAN: "The Company" means the railway company?

MR. SINCLAIR: It means the Canadian Pacific.

THE WITNESS: If the railways are to be operated, they have to obtain revenue adequate to their overall needs.

It is economically impossible to arrange that this or that item of traffic should be carried at a perpetually low rate without this condition inevitably forcing higher rates on other traffic, without affecting the argument that a continuation of the present low rates on grain must mean higher rates on other commodities, in view of the financial conditions of the two Canadian railway companies.

MR. SINCLAIR: Q. Now, at page 11 of the

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Pool Brief, the third complete paragraph, my lord.

THE CHAIRMAN: What is that?

MR. SINCLAIR: On page 11 of the Pool Brief, the third complete paragraph which reads:-

"Today, in the face of increasing world competition..."

You will note the fourth sentence in that paragraph which I now quote:-

"The railways are now being met with recurring demands for wage and salary increases and shorter hours, which to date they have not seen fit to resist."

I would ask Mr. Armstrong to let me have his comment in connection with that whole paragraph.

THE CHAIRMAN: It is the statement of fact which you wish to stress?

MR. SINCLAIR: Yes.

THE WITNESS: I shall assume first that the railways must make sure that none of their costs are out of line with those in the general economy.

The suggestion is made that railway wages and salaries are out of line. I do not know what the general economy is, but railway wages and salaries are somewhat higher or somewhat lower than other wages and salaries in what might be called urban industries as compared to agricultural.

I do not think there is any reason to complain about railway wages causing high freight rates on wheat. There is no more reason to complain about that than to complain about the wages in a combines factory making high prices for combines.

After all, the railway worker is no more a sinner in that

respect than the others. With due respect to the fact that we have sometimes found it necessary to point out that railway wages are, perhaps, on some occasions, a little high.

We have tried to rub it into our workers as best we can that we must not let railway wages and salaries get out of line with the general economy. We are doing everything we can, but even after that we are faced with a condition - not a theory - that we have to pay these wages.

To say that we have never sufficiently tried to resist these requests for higher wages just is not true, and it should not have been said. No one who wrote that could possibly have looked at the record.

The last increase in railway wages was a matter of public knowledge, and there could not be anyone in the room who is not familiar with what happened.

The argument reached such a point that at one stage the railway management had engaged in most elaborate and costly provisions for dealing with the suspension of railway service as a result of the strike.

For example, the guests in the Chateau Laurier Hotel were notified that they must be prepared to leave. And the guests at the Banff Hotel were notified that they were to move; and we had trains waiting to take them to the border before the dead-line of the strike.

We called in the unions and explained to them the necessary operations to make a shut-down possible, and with their co-operation, every arrangement had been made for a complete shut-down and it was only at the last moment, and with the greatest difficulty, that a compromise was arrived at.

THE CHAIRMAN: Have we not had that already?

MR. SINCLAIR: I think Mr. Crump dealt with it, if you will recollect.

THE CHAIRMAN: Yes. He gave us that.

THE WITNESS: Shall I make a statement?

THE CHAIRMAN: You make the statement that the railways did not resist properly to the demand.

MR. SINCLAIR: This Brief was prepared after the explanation had been made before this Commission by a senior officer of the Company, and when others of interest were present. Now, have you any further comments on that paragraph, Mr. Armstrong?

THE WITNESS: Yes. We are at the present time engaged in the most serious attempt to resist certain demands that are being made.

We have a large staff of officers busily engaged in producing evidence before at least two Boards. The conciliation Board dealt with the wage increases to the extent to which they were asked.

THE CHAIRMAN: How far have these proceedings gone?

MR. SINCLAIR: I think the rebuttal statements have been made and heard. I think that is as far as it has gone.

MR. SINCLAIR: There are two separate boards of arbitration?

THE CHAIRMAN: With the same Chairman?

MR. SINCLAIR: Yes, but the other two members are different. And written submissions were presented, and now, in accordance with a ruling, the rebuttal statements, which were also printed, have been made, and I think that is the situation now.

THE CHAIRMAN: Thank you.

MR. SINCLAIR: Q. Now, Mr. Armstrong, would you please comment on that statement that the railway wage levels should be fairly related to that of those who pay the freight? And I take that statement from the last paragraph on page 11, I mean from the incomplete paragraph.

A. Railway wage levels should be in accordance with the economic levels in general. Freight charges are not paid by one particular group of a community. They are paid by the community at large, and in some cases they are paid by others, in other countries.

The railway has to adopt a general policy of trying to keep all their wages in relation to the incomes of the population in general. They cannot expect, for example, that railway wages can be, let us say, in the case of railway workers moving wheat, halved, simply because the price of wheat is halved. We cannot distinguish the amount of time a man spends moving wheat from the amount of time he spends moving, let us say, harvest machinery, so we cannot say to a man: you must take less wages because you are moving wheat. But we can say: let us try to get our wage structure in general accord with the wage levels in the country at large.

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Q. Now, continuing in that paragraph at the bottom of page 11, and going over on to page 12, I quote from the brief -- this is the pool brief -- as follows:

"The Western farmer is not satisfied that this duty" -- that is, of keeping railway wages in accordance with the wages of those who pay the freight --

"has been fulfilled. Past wage increases have been made the basis of applications to the Board of Transport Commissioners for increased freight rates."

Would you please let me have your comment on that?

A. Well, that is quite well known, that the western farmer is inclined to grumble about this, but what else are the railway companies to do than they are doing? Can they do otherwise, when a wage increase is obtained by the usual processes of collective bargaining, in which we all believe so firmly, and which I do not think anyone is going to deny? Are we going to then say that because a wage increase has been incurred the railway companies cannot be compensated for it? What else could they do but ask for a freight rate increase as a result? The story goes on here to say that before they ask for an increase they should re-examine their wage and salary structure.

Q. That is at the very last of the top incomplete paragraph.

A. Now, suppose you said to the western farmer that before he demands a higher price for wheat or a lower freight rate on wheat he should re-examine the structure of farm wages and costs. Well, of course he is going to re-examine it all the time, with the idea of making another dollar, but equally surely he has got to face the costs that he has to face. If it costs him so much for a harvesting machine, he is going to have to pay that, and telling him that the harvesting machine company is charging him

more than he ought to pay is not going to help him. Telling me that railway workers are asking more than they ought to ask according to farm opinion is not going to help me. We are going to have to pay the wages, and the farmer is going to have to pay for the combine, and we will have to pay the prices for both those goods, economic goods, which are established by the usual processes of the market.

Q. Now I want to read to you the first complete paragraph on page 12.

COMMISSIONER INNIS: Before you start:

Q. Has there been any breakdown between wages and salaries?

A. In the case of the Canadian Pacific?

Q. Yes.

A. Oh, yes. Mr. Liddy has all kinds of figures on that. It is a case of arriving at what you mean by salaries, you know -- supervisory officials.

Q. How does it compare?

A. I am sure we could file something, couldn't we?

MR SINCLAIR: I think there was some evidence on that in one of the rate cases.

COMMISSIONER INNIS: The Canadian National too?

MR SINCLAIR: What do you mean by breakdown, Dr. Innis?

COMMISSIONER INNIS: Well, as to what proportion would be wages and what proportion would be salaries.

MR SINCLAIR: You mean as affected by these wage negotiations and wage increases?

COMMISSIONER INNIS: No, as I would suppose is meant in that sentence:

"It is submitted that before such a course of action is even contemplated, the Railways should re-examine

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their wage and salary structure."

I do not know what they meant, but it seems they had two things in mind.

MR EVANS: I do not think I have ever seen a breakdown between those who could be considered on a straight salary and those who are paid other than by salary, but the usual breakdown occurs at a level in these wage negotiations of say a chief clerk and downwards. SThe supervisory group is above, and the other group is involved in these wage negotiations. When the wage increase of we will say 17 cents an hour was awarded, those in the group of the chief clerk and under, including clerical, who are on salaries, those who are on an hourly pay basis, and those who are on a mileage basis, all got 17 cents an hour or the equivalent. Now, a special adjustment was made in the salaried classes, depending upon the salary arrangements, but not necessarily tied to the 17 cents.

COMMISSIONER INNIS: Have those figures been presented to the Board?

MR EVANS: I do not recall that they have. There was one exhibit filed, I think, in the last rate case---

MR MACPHERSON: The breakdown, Mr. Evans, I think was between organized and unorganized; that is the breakdown.

MR EVANS: I think Mr. MacPherson is quite right; and there was a breakdown in groups.

MR MACPHERSON: The final determination of the 20% Case, that was an exhibit.

MR EVANS: But I think fundamentally, Mr. MacPherson -- correct me if I am wrong -- the division there was those who were directly the beneficiaries of the increase that had been negotiated and those who were the indirect beneficiaries of it. My recollection of it was that the very large proportion of the total wage bill was

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in those directly benefiting. I can look that exhibit up.

COMMISSIONER INNIS: Does the Canadian National do the same?

MR EVANS: I have forgotten. They said not.

THE CHAIRMAN: Isn't this statement in the brief? Doesn't it merely mean this, that the railways should go over their whole wage list and salary list and see whether they cannot effect economies there that would take the place of the freight rates?

THE WITNESS: I think so.

MR EVANS: I think so.

THE CHAIRMAN: Then of course you say that these wages and so on are the result of transactions where you did resist, and you had to accept them.

MR SINCLAIR: Quite so.

THE CHAIRMAN: In that case it would not be much use going through them.

MR EVANS: There is an interesting fact, that during the depression there was a series of wage decreases put into effect.

THE CHAIRMAN: Yes, I remember that.

MR EVANS: And those were restored over a period of years as conditions got somewhat better. I rather suggest that that indicates that the company is aware of the desirable saving to be achieved through revisions both---

COMMISSIONER INNIS: That was paralleled by the increase in salaries, too, during the depression.

THE WITNESS: Yes.

MR EVANS: Well, I suppose there are normal progressive increases as seniority may demand or as positions changed, but those salaries that would attach to a particular position were rated lower.

THE CHAIRMAN: I think it is time to rise.

(Recess)

MR SINCLAIR: My lord, I think this might be a convenient time to file the breaking area, the breaking point area map that was discussed this morning. I have one copy for my friend Mr. MacPherson, that I am sure he will treasure and show to his friends in the same interest.

THE CHAIRMAN: Are you making an exhibit of it?

MR SINCLAIR: Yes, I thought that it might be better.

---EXHIBIT 209: Map of Canada, marked out in zones, showing rates on grain and grain products.

MR SINCLAIR: Q. Again looking at the pool brief for just a moment, Mr. Armstrong, this paragraph on page 12, the first complete paragraph, reads:

"The great proportion of the consumer goods used in the West are produced in the East, and the Transportation charges for these goods are passed on to the Consumers, and the farmer, the heaviest consumer, is already bearing the full brunt of these charges and all increases in them. Because he is farther in terms of rail miles from the world markets than are his competitors, he must himself absorb a very substantial part of the cost of transporting his grain to market."

THE CHAIRMAN: I note as you read that that, for the first time, I think, we are not told all of the cost. It says here that he must absorb a very substantial part of the cost.

MR SINCLAIR: Yes; that is why I am pointing it up, my lord.

THE CHAIRMAN: Whose brief is this?

MR SINCLAIR: This is the pool's brief.

THE CHAIRMAN: Perhaps we are arriving at that compromise that I have been praying for between the shipper and the consumer as to who pays. It is stated here that he pays a very substantial part of it.

MR SINCLAIR: Then we come to the next sentence: "The Western wheat farmer buys on the basis of cost plus freight while he sells his grain on the basis of world prices less freight."

THE CHAIRMAN: You are back to the same thing again.

MR SINCLAIR: I just point up, right in one paragraph of that brief, I just point up that little what might be called inconsistency -- might not; may require some explanation.

THE CHAIRMAN: It occurred to you too, did it?

MR SINCLAIR: Yes; I have got it marked here too, my lord.

THE CHAIRMAN: "The Western wheat farmer buys on the basis of cost plus freight while he sells his grain on the basis of world prices less freight."

MR SINCLAIR: Yes; and you will recollect, I think, Dr. Locklin's evidence in connection with the statement that the farmer pays the freight on everything he buys and everything he sells.

THE WITNESS: Do you want my comments?

MR SINCLAIR: He denied that.

THE CHAIRMAN: We know that Mr. Armstrong does not agree with this.

MR SINCLAIR: Oh, no. I was asking him if he had anything to add to what he has already stated in connection with that.

THE WITNESS: I could re-state everything I have

said, but the only thing that I really think might add a little light is the reference to Professor McDougall's evidence yesterday about the amount of freight increases, for example, which were passed on to consumers by dealers. It appears at 146 to 158 of our submission. As Professor McDougall said, we had these two men go out and do the best they could to find out the facts of the case, and they came back -- they certainly were given no instructions as to what to find; they were told what to look for, and they came back and they told us, no, you can't prove it, you can't show exactly what is passed on. I think farmers are no different from anyone else; sometimes they pay all the cost of what they buy, like consumers in general do, other times they do not pay at all, sometimes the manufacturer absorbs some, and so on. The error in this thinking is that you think of the farmer as always paying everything, the freight rates on everything that he sells and everything that he buys. Well, that would be a most unusual situation, and one that I do not believe exists. I think, broadly speaking, he pays the freight rate on what he buys, and, broadly speaking, he does not pay the freight rate on what he sells.

MR SINCLAIR: Q. I am now going to turn to the brief of the U.G.G., the United Grain Growers. Again, Mr. Armstrong, I take it that you have read it, studied it, the U.G.G. brief?

A. I have, sir.

Q. In large measure it presents arguments similar to those that we dealt with in the two briefs that we have considered, but I would ask you to turn on that brief to item 12 -- this is a numbered paragraph brief, in factum style -- page 12, item 12 or paragraph 12, and ask you, looking at that paragraph, which seemed to be underlining

the difficulties of the western farmers in periods of distress?

A. This is really a statement of the psychological attitude of the farmer, isn't it? That was the subject of the most complete agreement this morning between Major MacPherson and myself. The farmer thinks that this is all a case of his being robbed if the Crows Nest rates are raised and so on. It is psychological. Remember that there is justification for it if there was ever justification for wrong thinking on the part of human beings.

Q. You mean on account of the great and terrible stress that the western farm population went through, with the combination of economic difficulty and climatic adversity?

A. There can be no doubt about it, Mr. Sinclair; it was one of the most appalling events in economic history, and I certainly am the last to criticize western farmers for being sceptical, when even as honest a man as myself tells them that something is not going to hurt them. They have been hurt, but that does not change the fact that I am telling them the truth, you see.

Q. Quite so.

A. All I can tell them is, once again, that they were not being hurt by freight rates then, they were being hurt by an unkind world.

THE CHAIRMAN: What they are saying right here is that if freight rates had been increased then they would have been hurt.

THE WITNESS: I do not think they would have been then.

THE CHAIRMAN: Q. You say if rates had been increased then, that increase would simply have been added to the price, and they would have got the same thing anyway?

A. May I say, sir, I am not attempting to give you the details of my discussions with my clients at any time, but if anyone had asked me at any time during the great depression on the western plains whether this was a propitious time, even if we could get permission to raise the Crows Nest rates, whether it was a propitious time to raise them, I would have said, "Look, the farmer is wrong. This is not going to hurt him, but he thinks it is going to hurt him." Now, the farmer of Western Canada lost more more money out of being frightened in those years of the depression than he did out of anything else.

Q. Yes, I know; that is argument. What you are telling me is the fact, is it, that an increase in the rates if it had been made would not have affected the price of wheat to the farmer?

A. I think I can finish my statement. It might have in this sense, that so desperate was the psychological condition of the farmer at the moment that anything that looked like another burden thrown upon him, even if incorrectly, you see, might have added to that fright which led him to become so weak a seller.

Q. Added to that price?

A. To that fright, that alarm.

Q. Fright?

A. That alarm which caused him to be so weak a seller.

Q. Perhaps I used the word "fright"; I meant to use the word "price".

A. No, I am saying that.

Q. The statement made here is that if there had been an increase in freight rates it would have further reduced the price of wheat to the farmer?

A. In the indirect sense, sir, very indirect sense, and I hope you will be patient with me on this point. During

the great depression in prices of wheat, I have argued for years, and I continue to argue, I think with ample evidence to show that I was right at a time when it was not a popular stand, that nothing was worse as a factor in reducing the world price for wheat than the undue alarm of the western farmer, which led him to feel that he was ruined and that he had to let his wheat go for whatever it would bring. Now, I do believe that that psychological factor aided in depressing the price of wheat.

MR SINCLAIR: Q. You say that because the buyer was taking advantage?

A. Exactly. I used to go over to London and they would say to me, "Look, what are you talking about? The farmers in Western Canada, the grain trade, the pools, the government of Canada, all tell us that the world is flooded with wheat and that the farmer is lucky to live, and you say that is not so." Well, I say, I am alone, but still I think I am right. Now, if at that moment the good friends of the farmer, including the Canadian Pacific Railway, had undertaken to do something which frightened the farmer more, even if he were unduly and unjustly and improperly frightened, it would have been perhaps a further contribution to breaking the market for wheat, so in that indirect sense the statement is true, but in the direct sense that it would have been a direct market factor, oh no, it is not true.

THE CHAIRMAN: Q. Then it would not be a factor. We are back to where we started from. An increase in these freight rates would not have affected the return to the farmer for his wheat?

A. Except in that indirect fashion, that it might have alarmed him.

Q. Well, leaving that---

A. Directly, no.

MR SINCLAIR: Q. Now, Mr. Armstrong, you have indicated some of the differences between the wheat-growing economies of Canada and the United States so far as transportation is concerned, and you have put forward the view that at least some of the briefs of the western interests that have been filed with the Commission have misinterpreted the comparison. I am going to ask you to enlarge on the subject of the general comparison between the wheat-growing economies of the two countries as far as freight rates on wheat affect them, and in particular to deal with the point that Mr. MacPherson emphasized during his cross-examination of Mr. Jefferson, namely, that point that he put so strongly to Mr. Jefferson about the inter-mountain wheat in the United States?

A. The Oregon, Washington and Idaho crop. Well, I think that this whole subject really can only be understood, what I am going to say, if in following it use is made of a small outline map of the United States which I have had prepared and now should like to file.

MR SINCLAIR: I would like to file this as an exhibit, my lord. It will be Exhibit 210. It is an outline map of the United States, showing the states, and on certain of the states there are figures. I think it can be described as a map of the United States, showing in accordance with the legend the 1947 wheat crop in 18 chief producing states, in millions of bushels.

---EXHIBIT 210: Map of United States - 1947
Wheat Crop in 18 chief producing
states, in millions of bushels.

MR SINCLAIR: Opposite the figures are letters, W and S, W indicating winter wheat in millions of bushels, and S indicating spring wheat in millions of bushels.

MR MACPHERSON: Is this 1949 production, Mr.

Sinclair?

MR SINCLAIR: 1947 production.

Q. Now I would ask you, Mr. Armstrong, to speak to this exhibit 210 and tell us what it shows?

A. You will notice that this exhibit shows the production in the 18 chief producing states in that year. They accounted for $92\frac{1}{2}$ per cent of the total production. I did not attempt to deal with any state which produced less than 20 million bushels, because, after all, I could keep you here for weeks while I chased down what happens to a patch of wheat that is grown in Arkansas. I am dealing only with those states which produced more than 20 million bushels in that year. Now, 1947 is not chosen for any reason of malice, but because it happened to be the only year for which I had figures in detail available which I thought I could use. I have since then obtained the 1948 and 1949 figures in a similar way and looked them over, and, while of course there is a change from one year to another in different states, I am inclined to feel that you can depend on the 1947 map as being illustrative of the crops that have been going on for the last seven or eight years, with the exception that it happened to be a particularly large one.

Q. You say that 1947 was an exceptionally heavy yield in the United States?

A. 1,365 million bushels. Now, if you will look at that you will find that there are certain states which produce overwhelmingly of spring wheat -- I mean of winter wheat, and one region, one group of them, I would say, consists of Kansas, Texas, Oklahoma, Nebraska, Colorado, Ohio, Indiana, Michigan, Illinois and Missouri.

Q. Now, those states that you have named you say form one region?

A. Yes. I would like to call that region A for the purposes of this study. Those are the states which are situated, generally speaking, in or closely tributary to the great central plain of the United States, otherwise known as the Missouri-Mississippi River Valley. In 1947 these states produced 829 million bushels of winter wheat and 4 million bushels of spring wheat, or a total of 833 million bushels or 61 per cent of the total United States crop in 1947.

Q. Now would you discuss the wheat-growing economy in that region?

A. The plant oecology, which doesn't mean anything more than the conditions under which the wheat grows, is not uniform there. There is a great distinction between the moisture in the plains east of the Mississippi and the drier plains to the west, there is a distinction in agrarian economy, cultural practices and so on, between states, but marketwise, from the standpoint of market, I am inclined to think that we do no violence to the facts of the case by suggesting that all the wheat of that area, being all winter wheat, is largely interchangeable, with due respect for such considerations as that wheat from Missouri will be more likely to be fed, because of its quality, and the wheat from Kansas will be more likely to be milled.

(Page 18196 follows)

Q. What would you say as to the general markets for this wheat from the Winter wheat area, the Missouri and Mississippi valleys?

A. A proportion of the wheat grown in that area will be retained on farms for feed and seed, a unusually large proportion because of the fact that that is a very highly intensive livestock area, and in a livestock area there is a tendency to use more wheat especially of Winter wheat types. Quite a bit of it will be used there locally in the district for flour and mill feed, that will be very largely not shipped by rail at all, it will be moved by motor trucks chiefly, from the farms to small towns and other milling points.

Q. Do you know whether the rates on that would be around half a cent a bushel?

A. I fully expect that when the bulk of the crop will be sold out of the region as wheat flour, mill feeds, for consumption in the more thickly settled portions of the Union, or for export. Now, the part which is exported will move out chiefly by two channels, one, the Great Lakes-St. Lawrence Waterway from Chicago and other ports including Duluth, in some cases for some of it.

Q. And the other route?

A. Will be the ports in the Gulf of Mexico.

Q. And what happens to the wheat shipped by the Great Lakes-St. Lawrence Waterway?

A. That will move to Duluth, Chicago, or other Lake ports. It will move by inland water, perhaps even by the Canadian summer and winter ports in the East, out of Montreal and Halifax and Saint John, but more usually it will move out by the United States Atlantic ports

ranging from New York, Baltimore, Philadelphia and a few smaller ones. This grain will come to the Great Lakes by rail and then will move from Upper Lake Ports to Buffalo for furtherance to seaports. A lot of it will be milled in Buffalo after that journey for furtherance as flour to the great consuming centres of the Eastern United States.

Q. I would like you to put on the record, Mr. Armstrong, some representative rates for the rail movement of this wheat that we are discussing.

A. I would like to say that from now till the end of this discussion of the United States economy, I propose to use rates expressed in cents per hundred pounds to save confusion, and that I shall not further undertake the useless repetition of saying per hundred pounds. Each rate I quote will be a rate per hundred pounds in cents.

THE CHAIRMAN: Have we not already had all that?

MR. SINCLAIR: No, sir. This evidence should be most helpful to the Commission because it is directed to pointing out why we say that you can compare wheat in the United States and in Canada, and, in particular, to assist the Commission in assessing the viewpoints put forward mainly through Mr. MacPherson but also through some of these briefs: "Why talk about the United States wheat, that is winter wheat, it is ridiculous to come along with this kind of comparison." I think it should be most helpful to the Commission to have, and I propose with your consent to have Mr. Armstrong develop with some considerable detail the movements from these three economies, these wheat areas in the

United States where the wheat because of its markets and the rail rates, because you will recall Mr. MacPherson talking about the short wheat haul from the inter-mountain states, "Why, the State of Texas is right on the sea, practically," according to Mr. MacPherson, wheat moves practically for peanuts down there and the State of Washington is right there at the seaport as compared with the Saskatchewan farmer in the middle of this great land mass, who has to move his wheat these great distances to market.

THE CHAIRMAN: You want to show where the wheat moves to and the freight rates?

MR. SINCLAIR: Yes, sir.

THE CHAIRMAN: Is there any importance in the prices the farmer in the United States gets?

MR. SINCLAIR: We know the United States have been assisting their farmers, that is pointed out in one of these briefs, but in addition to that assistance, and apart from that assistance, the prices being received by the American farmer for his wheat have been higher than they have been under the Canadian Government.

THE CHAIRMAN: I am talking of the period before the war under open market conditions, how did prices vary then as between Winnipeg and Chicago?

THE WITNESS: In that period there was a very close relationship. Sometimes Winnipeg would be above Chicago, sometimes lower. They ^{varied} from time to time. There was a relationship and the general tendency was for United States wheat to be below Winnipeg.

THE CHAIRMAN: My point is really this: were these United States shippers paid Chicago prices less freight?

MR. SINCLAIR: Yes, sir, they have their markets, I think in some of the American rates, they take a Minneapolis price less freight or a Kansas City price, or Galveston, Texas, but I think, sir, that we are prepared to show, and I think that this should be, as I say, I can hardly understand it to be a surprise to my friend, but the impression was left here during the cross-examination of Mr. Jefferson that the American farmer was a singularly fortunate individual in the fact that he had such short hauls to water for his wheat.

THE CHAIRMAN: To water?

MR. SINCLAIR: Yes, either the Gulf Waterway, and again I emphasize this, a particular inter-mountain wheat area where there is a considerable development of white wheat.

THE CHAIRMAN: It may be worthwhile looking into this question of prices.

Have you done that, Mr. MacPherson?

MR. MACPHERSON: I propose to file information on that.

MR. SINCLAIR: I suggest if Mr. MacPherson is going to file information, he could let me have it now so I can take a look at it tonight.

MR. MACPHERSON: I think I will have it in such form as I can show you tonight.

THE CHAIRMAN: Yes, the sooner, the better.

THE WITNESS: It will be noted that Kansas alone accounts for over 20 per cent of the whole United States wheat crop. This is a winter wheat state in this region we are discussing.

THE CHAIRMAN: How does that compare with Saskatchewan?

THE CHAIRMAN: How does it compare to Saskatchewan?
Saskatchewan has done better than that sometimes?

MR. SINCLAIR: Oh, yes. I do not know. I think we have some figures here.

THE CHAIRMAN: Saskatchewan is generally much better than that, I think.

MR. SINCLAIR: Better than two eight seven million.

THE WITNESS: I would not think much better. It could not have been much better. I feel quite positive of that.

MR. SINCLAIR: What is the Exhibit?

THE CHAIRMAN: What about 1928.

MR. FRAWLEY: In 1928 it was 303 million for Saskatchewan.

THE CHAIRMAN: Yes, and what about in a more recent year?

MR. SINCLAIR: The highest in recent years was 1942, when it was 335 million. Then it went down to 168 million in 1945. I have been looking at page 103 of the Appendix to Part I of the Canadian Pacific Brief where it shows the Saskatchewan production.

THE CHAIRMAN: I think that is right. The highest Saskatchewan yield up to date is 335 million bushels.

MR. MacPHERSON: That is right, 1942, my lord.

COMMISSIONER INNIS: What about 1947?

MR. SINCLAIR: It was 103 million. And in that year, I think it might be of interest to know, Alberta had 103 million and Manitoba had 43 million.

THE WITNESS: Starting with Kansas points, we picked some in order to give the main shipping points at what we regard as duplicate distances, distances which we

could compare with similar distances in Canada if necessary.

I shall not make a comparison between individual rates in the States and similar rates in Canada. I am merely trying to build up the whole United States rate picture as against the whole Canadian rate picture.

From Holliday to Chicago, a distance of 465 miles, the rate is 57¢.

From Salina, Kansas, to Chicago, a distance of 669 miles, the rate is 50¢.

From Hartland, Kansas, to Chicago, a distance of 869 miles, the rate is 59¢.

From Holliday, Kansas, to Duluth, a distance of 768 miles, the rate is 50¢.

From Salina, Kansas, to Duluth, a distance of 963 miles, the rate is 63¢.

From Hartland, to Duluth, a distance of 1,173 miles, wheat has been known to move at a rate of 72¢.

From Medill, Missouri, to Chicago, a distance of 264 Miles, the rate is 26½¢.

From Medill, Missouri, to Duluth a distance of 728 miles, the rate is 56½¢.

MR. SINCLAIR: Q. As to these rates you are giving us, are they rates which are presently in effect?

A. Yes, they are rates which are presently in effect, and I would draw attention to this: I am not going to make comparisons all the way through.

You will note that the rate from Medill, Missouri, to Chicago, a distance of 264 miles, the rate was 26½¢, which was ½¢ per hundred above the rate from Edmonton or Calgary to Fort William.

COMMISSIONER INNIS: Is it possible that wheat would be shipped from Kansas to Duluth?

MR. SINCLAIR: Some of it does move that way.

COMMISSIONER INNIS: But does very much?

MR. SINCLAIR: Oh, no, we are not saying that that is the way the main movement is.

THE CHAIRMAN: Q. Could Mr. Armstrong tell us where the Kansas wheat goes?

A. It goes everywhere in the United States for all sorts of purposes.

Q. I did not mean that. Is much of it shipped to Chicago?

MR. SINCLAIR: No, sir. I think you would find it would go to the Gulf Ports.

THE CHAIRMAN: Are you giving us rates to the Gulf Ports?

MR. SINCLAIR: Yes.

THE WITNESS: Now we will have some rates to the Gulf Ports. A great deal of the wheat goes to the Gulf Ports.

MR. SINCLAIR: Maybe we could go to New Orleans, first?

A. Tuscola, Illinois, for a distance of 776 miles, the rate is 39¢.

Pine Bluff, Arkansas, for a distance of 420 miles, the rate is 26½¢.

I did not find any export rates to ports in the United States under 26½¢. A great deal of the grain exported from this area goes out via Galveston, Texas.

It might be of interest to the Commission to give them a fair picture of this as well. Note that in most years Galveston and Houston are combined.

MR. SINCLAIR: Q. You mean Houston, Texas?

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A. Yes. Galveston and Houston are one port for all practical purposes. They handled more than 25% of the total exported from the United States, and more than the total exported from New York, Philadelphia and Baltimore. That is quite startling. There is an enormous movement there. That is the way Kansas and Texas wheat goes out, by New Orleans, by Galveston, and Houston, which is even more important.

THE CHAIRMAN: Q. Does it go all by rail?
Or does it go by river?

A. Some goes by rail and some goes by river. But the most of the movement, we understand, is by rail.

MR. SINCLAIR: Q. These are the rates for export on grain movements?

A. That is right.

THE CHAIRMAN: Does that mean that they are lower than the domestic or higher?

MR. SINCLAIR: The evidence is that there are rates in the United States for domestic movements within certain areas.

THE CHAIRMAN: You are going to give us the export rates?

MR. SINCLAIR: Yes.

THE CHAIRMAN: Which are lower than the domestic?

MR. SINCLAIR: Yes.

THE WITNESS: Quite!

THE CHAIRMAN: All right.

THE WITNESS: To Galveston the rate from Rutledge, Missouri, a distance of 1242 miles, is 36¢.

From Newton, Kansas, for a distance of 776 miles, the rate is 55¢.

From Standart, Texas, for a short haul of 420 miles, the rate is $52\frac{1}{2}\phi$.

From Purcell, Oklahoma, for a distance of 420 miles, the rate is $52\frac{1}{2}\phi$.

The domestic rates for movements to the Gulf Ports run 25% to 30% higher than that, and they scarcely come into this argument.

MR. SINCLAIR: Q. Would those rates illustrate the prevailing rates in what you have described as region "A"?

A. I think so. I say that where wheat from region "A" is moved to Minneapolis for furtherance to domestic markets, the rates will be on the domestic basis and, again, higher than those export rates I have been quoting.

I think that is a fairly good picture of the rates on export movements and domestic movements, as they affect the wheat from that great area I have described.

Q. What is the next region you wish to discuss?

A. The next region which I shall call "B", consists of spring wheat deliveries in the states of Minnesota, North Dakota, South Dakota and Montana.

In this area plant ecology and agricultural economic conditions are uniform, generally speaking, as in the same sense as in our own Prairie Provinces.

While the type of the wheat is mostly hard spring, nevertheless one part of Manitoba grows a very excellent grade of winter wheat.

Q. What was the production in this area for 1947?

A. For region B in 1947, the production was 32 million bushels of winter wheat; 253 million bushels of spring wheat, making a total of 285 million bushels, which

amounted to 1% of the total United States wheat crop.

Q. Of the total United States wheat crop?

A. Yes.

Q. And what, in general, is the normal market for the wheat from this region?

A. This wheat is high grade marketing wheat, and as the Provincial Submissions and the United Grain Growers' Submission - -

Q. You mean the three Prairie Provinces on grain?

A. Yes; it is in active demand for marketing in the domestic market in the United States, although it is not enough to fill that market.

Some of it is used on farms for feed and for seed, and I think it would be reasonable to say that the proportion of it which is used for feed and seed would be about the same as in the Prairie Provinces, because the type of agriculture in the two regions is not unlike.

So a small proportion of it would be milled for local consumption in the Spring Wheat States.

The Canadian Pacific Submission has demonstrated....

Q. That would be in our Brief, Part I, page 43.

A. That the percentage of non-agricultural to the total population in the Spring Wheat States is considerably less than in our Prairie Provinces, and it is decreasing; while the percentage in our Prairie Provinces is larger than in the Spring Wheat States, it is increasing; so that means that the percentage of the wheat crop milled locally for local consumption will almost certainly be less in the Spring Wheat States than in our Prairie Provinces.

Q. That is a trend you are talking about?

A. Yes.

THE CHAIRMAN: How does the present population compare in those two cases?

MR. SINCLAIR: We have put that in in Professor McDougall's submission.

THE CHAIRMAN: Very well. You can let us have it tomorrow morning.

We shall adjourn now until tomorrow morning.

---At 4.45 p.m. the Commission adjourned until tomorrow, Thursday, March 16, 1950, at the hour of 10.30 o'clock in the forenoon.

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